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MONTHLY PROJECTIONS
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HOW SLOW IS ECONOMIC GROWTH ANYWAY?

Although the index of hours worked increased in September, these gains were the result of a rebound in the workweek. August's decline in the workweek appears to be associated with hot weather rather than underlying economic conditions. Therefore, the extension of the workweek in September has little economic implication. On the other hand, only a little more than 50% of all industries registered increased employment while the industrial production index was flat. After adjustment for inflation, consumption declined in September. Our monthly indicators show a slight dip in estimated GNP for September. Even growth in employment was distorted by an unusually large 115,000 increase in local government workers. Excluding government, employment grew less than 100,000.

Credit market conditions showed only fleeting signs of weakness. Some short-term interest rates rose, although yields on commercial paper declined slightly from the previous month. However, long-term interest rates eased modestly. More significantly, money growth came to a halt. If the Federal Reserve was following an interest rate target, as increasingly appears likely, reduced money demand would be reflected in slower money growth. Also, even though interest rates did not reveal the weakening state of the economy, flattening in the growth of monetary aggregates definitely did. There has been virtually no growth in checkable deposits during the past three months and only negligible growth in small time deposits.

Indeed, the 2.2% growth in third-quarter GNP is consistent with this pattern of weakening economic activity as the quarter progressed. Our estimates suggest that real GNP in September was below its third-quarter averages. Even if economic growth rebounds in the next few months, nonfarm GNP growth in the fourth quarter will be hardpressed to even reach third-quarter levels.

That economic activity has slowed significantly should require no dispute. What has caused the slowing requires some more substantial thought. Tough mone-

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tary policy has received much of the credit for reduced expansion of economic activity. Certainly, interest rates began rising early in the spring. Those higher interest charges could have begun weakening activity by late summer (of course, the overt policy tightening by the Federal Reserve in August when they increased their discount rate almost certainly cannot be credited with slowing the economy as soon as September. Such a quick response to changes in monetary policy simply have not been empirically verified.) If monetary tightening is responsible for economic slowing, then further slowing may surface. At this point, there is little evidence that the monetary authorities have shifted their policy thrust. Of course, further restraint in an economy that no longer is moving forward could rapidly deteriorate into an unintended recession.

Already, inventories are beginning to grow rapidly at the retail and wholesale level. While most of the inventory expansion during the summer appears to be another increase in automobile inventories, more sinister interpretations of the rapid inventory growth can be made. Certainly, some unintended inventory investment has occurred in the summer months. Thus, weakness in the economy during the fall as manufacturers restore inventories to an appropriate balance with slowing orders and reduced sales potential is not out of the question.

A more likely candidate for the recent economic slowing is the reduction in export flows as previously shipped American goods were being accumulated in warehouses abroad. This inventory excess is not measured in national statistics. However, its impact is readily apparent in the significant slowing of export flows. During the third quarter, exports grew 8.4% after inflation adjustment, but these estimates are subject to significant revision. In particular, the export growth is heavily dependent upon a spurt in export activity during August. However, as all categories of both exports and imports spurted in that month, it is possible that better processing of data rather than increasing trade flows accounted for the spurt. If so, activity will fall back in September and the third-quarter estimates will be revised downward.

Some slowing also occurred as a result of reduced defense activity. Reductions in defense budgets over the past two years have finally begun to restrain the growth of defense expenditures. As these reductions are continuing, further weakness in the defense component of government should be anticipated in the next few quarters.

If slowing is the result of an adjustment of inventories abroad, the slowing should soon be coming to an end. Of course, continued weakness in defense spending and the impact of monetary restraint upon consumer spending should surface later this year or early next year. Therefore, no significant acceleration of economic activity should develop. Nevertheless, some signs of a rebound in activity soon should be apparent.

At the present time, the only evidence that the economy is doing a bit better than its slight decline in September is the drop to a cyclical low of 1.9% for the insured unemployment rate and a slight uptick in business loans.

On the other hand, of the six industries that previously had reached cyclical peaks, four have now experienced some easing in their capacity utilization. Only the aerospace industry as a result of strong orders for commercial aircraft and the chemicals industry continued to show significant utilization pressures from that original group. On the other hand, two new industry sectors, non-electrical machinery and fabricated metals, have also reached cyclical peaks. If their experience follows that of the previous industries with capacity constraints, industrial materials associated with their activities will begin experiencing accelerated price pressures. On the other hand, price pressures in the textiles, paper, and plastics industries, all of which previously experienced significant pressures, should ease. The net effect upon industrial inflation should be little changed as a result of these utilization shifts.

Of course, excess production of oil remains the major industrial material pricing event. Oil prices still are expected to rebound during the heating season and then collapse as early as February. The collapse in prices could bring oil down to $10 to $11 per barrel by March. Then, some regrouping in oil prices is anticipated with prices firming as the next heating season approaches. On balance, we are assuming that OPEC will produce close to 20 million barrels per day next year and that such a supply can only be absorbed with prices in the United States averaging $14 per barrel. On average, this would be a drop from the $16 per barrel average that oil commanded in 1988.

Also, labor markets are becoming increasingly tight. While wage pressures remain remarkably subdued, the hourly earnings index is beginning to accelerate. Even the employment cost index is beginning to show some acceleration from a year ago. At the same time, the reduction in productivity gains that normally occurs near cyclical peaks appears to be developing again. Our preliminary estimates suggest that productivity fell 1% at annual rates during the summer months. Thus, a gradual increase in unit labor costs is developing. The combination of rising demand pressures in those industries with high utilization rates and gradually rising cost pressures for all industries should lead to higher inflationary pressures.

Of course, the decline in oil prices will offset these normal upward pressures early in 1989 if our analysis is correct. By mid-year, however, inflationary pressures in excess of 5% should reappear. That would be the time when Federal Reserve restraint again would develop. Interest rates then would move higher and economic activity once again would slow.

Quarterly Profile of GNP

	1988-2	1988-3	1988-4	1989-1	1989-2	1989-3	1988 Annual	1989 Annual
Real:	3.0	2.2	2.2	3.8	3.2	1.7	3.8	2.9
Price:	5.5	4.4	4.0	3.7	4.0	4.5	3.3	3.8
Nominal:	8.7	6.7	6.3	7.7	6.3	6.1	7.2	6.8

Monthly Statistical Highlights for October 1988

Payroll employment +200,000; index of hours worked +0.2%; household employment +259,000; civilian unemployment rate 5.4%; personal income +0.6%; savings rate 4.2%; personal consumption +0.6%; retail sales +0.8%; auto sales 10.4 million units; housing starts -0.8%; housing permits -0.9%; construction expenditures -0.1%; business inventories +0.5%; orders for durable goods +1.3%; orders for nondefense capital goods +1.6%; industrial production +0.3%; CPI +0.3%; PPI -0.1%; consumption deflator +0.3%; leading indicators +0.3%; currency index -3.6%; equity index +3.1%; real GNP(AR) +2.7%; M1(AR) +2.8%; M2(AR) +2.2%.

Monthly Statistical Highlights for November 1988

Payroll employment +302,000; index of hours worked +0.2%; household employment +322,000; civilian unemployment rate 5.3%; personal income +0.6%; savings rate 4.2%; personal consumption +0.6%; retail sales +0.7%; auto sales 10.6 million units; housing starts +1.8%; housing permits +0.5%; construction expenditures +0.6%; business inventories +0.6%; orders for durable goods -0.6%; orders for nondefense capital goods -2.3%; industrial production +0.3%; CPI +0.3%; PPI +0.2%; consumption deflator +0.4%; leading indicators +0.2%; currency index -4.4%; equity index +3.4%; real GNP(AR) +4.3%; M1(AR) +4.7%; M2(AR) +7.4%.

Commentary

Employment - Reductions in initial unemployment claims continue to suggest more than normal expansion in employment for October. Thus, an increase in employment in the private sector of at least 260,000 is anticipated. On the other hand, the unusual spurt in government employment during August and September probably was the result of seasonal distortions. These distortions either will be adjusted by reducing the September estimates for government, causing further increases in employment for October, or by reversing the September estimates in the October survey. In either case, the level of October employment probably will be close to what we anticipate. However, if government is reversed rather than revised downward, the change in payroll employment for October will be less than normal, approaching only 200,000. Then, a continuation of relatively strong employment gains should occur in November, leading to a return to robust employment gains in that month.

It is now clear that a rebound in hours worked during September was merely the regaining of a normal workweek following an August aberration. That unusual behavior may have been the result of the heat wave that gripped the country during August survey week.

One factor suggesting less than normal employment gains ahead is the poor performance in productivity early in 1988. Such reductions in productivity usually suggest that overhiring has occurred and that slower growth in labor demand can be expected in the months ahead.

Personal Income and Outlays - Personal income grew slightly less than anticipated in September, but all of the weakness was the result of further declines in farm income. Apparently, neither crop insurance nor subsidies were distributed in that month. In the remainder of the year, however, subsidies should increase significantly. As a result, personal income should begin growing sharply.

One component of personal income already growing sharply is the personal interest expense. There has been a spurt in short-term interest rates that clearly has added to property income. If interest rates now are to stabilize for the next few quarters, a slowing in property income gains should be anticipated. As a result, wage and salary growth probably will be growing faster than personal income gains over the next year.

Auto sales slipped early in October, as expected, but quick introductions of dealer inventories should cause a rebound in unit sales later in the month. A sharp increase in auto sales despite a reduction in units is the result of increased prices for new cars. Although the drought has substantially accelerated purchases of nondurable goods, especially foods, falling oil prices soon will cause the nondurable component to grow more slowly. Similarly, reduced energy prices will be reflected in the transportation services and utilities components of services expenditures. This should lead to slower growth in service spending than anticipated in our previous forecast. On balance, consumer spending is expected to grow a modest 2.0% after adjustment for inflation next year. This compares with a 2.4% rate of growth in the past six quarters, which is down from a 4.5% growth path in the first four years of this economic expansion. Clearly, consumer activity is no longer pulling this economy forward.

Construction - Our outlook on housing has changed very little in recent months. Slower gains in interest rates than originally expected lead to slightly higher activity for single-family homes in the fall and winter months than had been anticipated. When interest rates rise, however, single-family starts begin to fall significantly later in 1989. No recovery is expected for apartment construction over the next year. Growth in nonresidential construction is largely the result of warehouse and industrial expansion. Some lodging expansion also is anticipated. On the other hand, office buildings should continue to trend downward into 1989. The current outlook for construction is decidedly for less activity than was expected in our August forecast.

Of course, some of this slowing is the result of reduced growth in the construction cost index. This index has grown at an annual rate of less than 2% in the past five months and is expected to continue growing at only a slightly accelerated rate in the next year.

Business Activity - A rebound in business inventories in July along with larger than anticipated expansions in August have led to slightly higher inventory holdings than originally anticipated. However, manufacturing inventories remain behind anticipations. Most of the inventory expansion is currently occurring in durable retail activity. This largely reflects earlier shipments of new model cars than traditionally. At the present time, production schedules suggest that automobile makers desire this increased inventory and that little correction for inventory excesses are necessary at the present time.

Orders for durable goods have been unusually choppy in recent months as a result of aircraft orders. Some very large aircraft orders have swelled the indices, which then flow back toward normal when no unusual aircraft orders surface. As many aircraft companies already have ordered their next fleet, subsequent surges in orders for durable goods are not anticipated. On the other hand, the computer industry is creating significant confusion by its recent battle over appropriate information-carrying technology. Uncertainties associated with these technological battles have led to reductions in computer orders. This issue probably will be resolved in the next few months and orders will again spurt. In the meantime, sluggishness in computer orders is beginning to be reflected in reduced activity and shipments as well.

Industrial production was flat as a result of a sharp decline in utility production following a summer heat wave. Autos were assembled at 7.4 million units and are expected to rise to assemblage rates approaching 8 million units in the fall. This should provide a significant area of strength to the industrial production index. In addition, continued 0.4% - 0.6% monthly gains in production for business equipment and modest increases in production of industrial materials assures continued growth in the industrial production index through the remainder of this year.

Defense shipments are expected to remain low during the fourth quarter and then gradually build during the first half of 1989. In real terms, there will be minimal increases in defense expenditures.

Prices - Because of the direct and indirect influences of falling oil prices, our inflation estimates all are growing at a slower rate than originally anticipated with the exception of the GNP deflator. The more rapid growth in the GNP deflator appears to be the result of shifting compositions from changing expenditures. Also, the current weakening of import prices has probably biased the GNP deflator upward. An upward bias in this deflator is expected over the next year. This would reverse the decidedly downward bias experienced by the deflator in the past two years.

Miscellaneous - Merchandise trade balances have been converted into the customs value for imports. As a result, the current expectations are not really comparable with the forecast. In fact, since the adjustment leads to about a $1 billion reduction in the trade balance, we are actually increasing our estimates of trade deficits. Obviously, the higher trade deficits than originally projected result in greater weakness in the dollar's value than previously expected. By next April, when our currency index is expected to reach its low of 87.7, the yen probably will be trading at 110 to the dollar while the German mark probably will be trading at 1.65. Although deficits do not grow sharply beyond that period of time, increasing interest rates in the United States as the Federal Reserve begins to fight inflation leads to the dollar's strength. Of course, such premature strengthening will stabilize trade balances, causing slowing in the growth of economic activity.

Our current estimates suggest that adjusted profits will rebound from their summer slump and reach a peak next March. As interest rates on long-term government bonds are expected to change very little over that period, these improving profits lead to improving market values for equities. Indeed, our estimates suggest a relatively strong equities market through most of 1989.

Falling oil prices should substantially reduce the inventory valuation adjustment over the fall and winter months. As a result, the quality of profits rises significantly. In addition, inventories do not generate substantial credit market pressures.

FINANCIAL MARKETS

This year's government deficit was $155.1 billion, up from slightly more than $150 billion a year ago. What is troubling about this result is the fact that economic activity during the budget year grew nearly 4%. Thus, the structural deficit appears to have worsened slightly during the year. As the economy grows more slowly next year, receipts will continue to slow. Indeed, the household sector will receive a significant tax reduction as marginal rates are reduced to 28%. As the corporate sector already is experiencing most of its offsetting tax increases, it appears that the 1986 tax reform package may not have been neutral but actually a slight tax cut. This appears to be why the structural deficit has not been improving despite significant restraint in defense spending. The evidence strongly suggests that growth will not be sufficient to resolve the deficit problems.

Government deficits may rise slightly during this period of reduced economic growth, but the deficits should again be trending downward in the spring and summer of 1989. Reduced payments for agricultural supports and reduced outlays for petroleum purchases should be largely responsible for this modest budgetary improvement. In addition, interest rates are not expected to change significantly, so the interest burden should not rise significantly. Thus, although the government probably will be placing increasing strain upon the credit markets, we can assume basic neutrality from their borrowing efforts.

The household sector will be gradually reducing housing purchases, slowing installment credit growth and increasing savings rates. All these factors lead to increased sources of funds to the credit markets, which would generally lead to reduced interest rate pressures. However, the movements, although in the right direction toward lowering interest rates, are not significant.

The corporate sector actually increased some inventory-related borrowings along with fixed investment borrowings during the spring and summer months. As a result, interest rate pressures intensified. If inventories are to be more moderately accumulated in the fall, as expected, and if fixed investment is to grow more slowly, then the corporate sector will need slightly less funds than originally expected. In addition, corporate profitability is expected to gradually improve. Thus, the generation of funds should grow slightly faster than the need for funds, leading to a slight moderation of interest rate pressures.

Some people have been concerned by the significant increase in low-quality corporate debt because of massive corporate restructuring. Obviously, that debt creates problems for that class of debt instrument, which may be growing more rapidly than the ability of traditional high-yield investors to absorb the additional paper. As a result, interest rates on junk bonds should rise relative to overall interest rates. In addition, increased credit risk associated with unexpected restructuring appears to be increasing the interest rates of all corporate issues. However, these interest rate adjustments appear to be relative to other debt instruments. At some point, the conversion of equity into debt must raise interest yields relative to the value of equity. Thus, a differential return between equities and corporate indebtedness should materialize. The net result would be higher interest rates and reduced equity financing costs. But this effect may be offset by the increased volatility and risk generated by the high leveraging of some corporations. At this time, there appears to be an argument suggesting that corporate restructurings are leading to higher interest rates than otherwise would prevail in the corporate sector; but the effects do not appear to be very large.

While the sources and uses of funds suggest that there will be a slight reduction in the domestic savings deficiency over the next year, it is not clear whether the savings imbalance will fall sufficiently to encourage foreigners to continue providing their savings at unchanged interest rates in the United States. The absence of further improvement in the trade balances suggests that foreign investors will increase their reluctance to provide savings in our country. If so, interest rates could rise slightly over the next six months. However, the strongest case probably is for a slight downward drift in long-term rates because of the reduction in inflationary pressures that are anticipated as long as oil prices are falling. Later next year, when the dollar comes under attack and inflationary pressures rise at nearly the same time, higher interest rates will be necessary to continue attracting funds from abroad. Indeed, the Federal Reserve is expected to raise the discount rate again before the end of next spring. These increased interest rate pressures should initially be reflected throughout the yield curve.

Equity Markets - The near-term outlook for equity values is favorable. Interest rates are expected to remain unchanged or actually trend down slightly. The current sluggishness in the domestic economy is expected to give way to renewed modest growth. Because oil prices will be falling, the inventory valuation will not be as dramatic an adjustment as earlier in the year. Thus, the quality of corporate earnings will rise. The one fly in the ointment is reduced attractiveness of American assets by foreign investors. This would suggest that the big name companies could begin to underperform the overall market. Nevertheless, our basic valuation formulas suggest that equity values could rise significantly over the next six months. The Dow Jones index should easily exceed 2200 in the next few months and probably could approach 2300 by spring. When interest rates begin rising, however, a slowing economy will begin to erode corporate profitability. At that time, equity values should be trending downward.

Some interest-sensitive securities should perform better than average in the near-term environment. This suggests that regional banks and utilities should receive attention. As the dollar weakens, however, some of the multinationals which have lagged behind market performance in recent months should again come to the fore. Of course, the industries which are beginning to feel capacity utilization pressures also should perform well. Thus, chemicals, fabricated metals, nonelectrical machinery, and commercial aircraft companies all should outperform the market in the next six months.

EMPLOYMENT

	Payroll Employment		Index of Hours Worked		Household Civilian Employment		Civilian Unemployment Rate		Hourly Earnings Index	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1988	105281	105281	125.1	125.1	114713	114713	5.4	5.4	178.0	178.0
May	105502	105489	124.4	124.4	114195	114195	5.6	5.6	178.6	178.7
June	105848	106057	125.3	125.4	115018	115018	5.3	5.3	178.5	178.6
July	106075	106271	125.6	126.4	115127	115059	5.4	5.4	179.3	179.3
August	106295	106440	125.9	125.5	115226	115180	5.4	5.6	180.1	179.6
September	106560	106695	126.1	126.0	114974	115328	5.3	5.4	180.8	180.4
October	106753	106895*	126.3	126.3*	115543	115587*	5.3	5.4*	181.3	180.8*
November	106900	107197	126.5	126.6	115881	115909	5.3	5.3	181.8	181.5
December	107048	107536	126.7	127.0	116220	116257	5.2	5.2	182.4	182.0
January 1989	107309	107790	127.0	127.3	116489	116533	5.1	5.1	183.2	182.6
February	107627	108081	127.4	127.6	116750	116810	5.0	5.1	184.0	183.3
March	107948	108344	127.7	127.9	117012	117093	5.0	5.0	184.8	183.9
April	108062	108541	127.8	128.1	117143	117327	5.1	4.9	185.3	184.6
May	108174	108729	128.0	128.3	117292	117543	5.0	4.9	185.9	185.3
June	108290	108851	128.1	128.4	117453	117677	5.0	4.8	186.4	186.0
July	108483	109029	128.3	128.6	117638	117890	4.9	4.8	187.2	186.6
August	108754	109142	128.6	128.7	117837	118035	4.9	4.8	188.0	187.3
September	109021	109245	128.8	128.8	118030	118172	4.9	4.9	188.8	188.0

PERSONAL INCOME

	Personal Income		Wage & Salary		Personal Savings		Disposable Income		Personal Outlays	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1988	3.996	4.001	2.394	2.394	89.5	97.9	3.352	3.358	3.263	3.260
May	4.014	4.021	2.407	2.408	152.4	151.7	3.434	3.442	3.282	3.290
June	4.042	4.045	2.425	2.428	149.8	133.9	3.463	3.465	3.313	3.331
July	4.064	4.071	2.440	2.452	145.3	141.0	3.475	3.487	3.329	3.346
August	4.087	4.083	2.453	2.457	140.2	132.4	3.483	3.497	3.343	3.365
September	4.110	4.103	2.466	2.471	127.0	147.5	3.488	3.513	3.358	3.366
October	4.132	4.127*	2.478	2.484*	134.3	148.0*	3.509	3.534*	3.375	3.386*
November	4.153	4.153	2.490	2.501	144.5	148.1	3.537	3.556	3.393	3.408
December	4.175	4.180	2.502	2.518	153.8	149.7	3.565	3.580	3.411	3.430
January 1989	4.192	4.197	2.521	2.533	158.5	155.7	3.590	3.602	3.431	3.446
February	4.231	4.224	2.543	2.551	154.3	156.7	3.605	3.626	3.451	3.469
March	4.270	4.249	2.565	2.566	148.9	158.5	3.621	3.647	3.472	3.489
April	4.286	4.275	2.574	2.582	149.4	162.9	3.641	3.667	3.492	3.504
May	4.298	4.301	2.584	2.597	143.7	166.9	3.656	3.688	3.512	3.521
June	4.311	4.325	2.593	2.611	136.8	172.4	3.672	3.710	3.533	3.538
July	4.339	4.348	2.610	2.625	139.4	172.9	3.691	3.730	3.552	3.557
August	4.368	4.374	2.627	2.639	139.3	174.4	3.710	3.752	3.570	3.578
September	4.396	4.399	2.645	2.652	140.4	177.2	3.729	3.773	3.588	3.596

Fore. = August Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

CONSUMPTION

	Personal Consumption		Durables		Nondurables		Services		Consumption Real	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1988	3164.2	3161.3	442.3	442.6	1025.7	1025.7	1696.2	1693.1	2565.9	2562.5
May	3182.7	3190.9	445.0	447.4	1030.3	1038.2	1707.5	1705.3	2569.7	2574.3
June	3213.5	3231.5	453.6	459.3	1034.8	1046.0	1725.2	1726.1	2587.1	2600.3
July	3226.4	3245.3	450.9	454.4	1039.2	1053.0	1736.3	1737.9	2587.3	2600.0
August	3244.5	3263.4	454.5	454.8	1043.1	1059.6	1746.9	1749.0	2593.5	2608.1
September	3255.4	3264.1	455.4	451.7	1047.3	1060.0	1752.7	1752.4	2593.9	2595.8
October	3273.2	3283.7*	456.3	454.3*	1051.5	1064.7*	1765.4	1764.7*	2597.8	2601.1*
November	3290.8	3304.9	457.1	459.4	1056.1	1069.2	1777.6	1776.3	2601.4	2607.4
December	3308.7	3326.6	458.2	462.6	1061.0	1074.6	1789.5	1789.4	2605.3	2616.3
January 1989	3328.2	3342.0	459.5	462.0	1066.4	1078.9	1802.3	1801.1	2610.4	2619.3
February	3347.5	3364.4	460.6	465.3	1071.1	1084.9	1815.8	1814.2	2613.2	2626.2
March	3365.4	3383.0	461.7	467.1	1075.8	1090.6	1827.9	1825.3	2614.9	2630.4
April	3385.7	3398.0	461.9	466.9	1083.4	1093.9	1840.4	1837.2	2616.5	2632.5
May	3405.8	3414.5	461.5	467.4	1091.2	1098.2	1853.1	1848.9	2617.8	2635.5
June	3429.5	3430.3	464.7	466.2	1099.0	1103.6	1865.8	1860.5	2621.9	2637.2
July	3444.4	3449.2	461.0	469.8	1104.5	1107.6	1878.9	1871.8	2623.3	2640.5
August	3464.3	3469.1	462.9	471.0	1109.9	1113.8	1891.5	1884.3	2628.5	2645.1
September	3482.0	3486.7	464.2	470.3	1114.4	1119.6	1903.4	1896.8	2629.9	2647.2

RETAIL SALES

	Retail Sales		Non-Auto Durables		Auto (Million Units)		Nondurable Sales		Auto Sales	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1988	131.72	131.72	20.85	20.85	10.5	10.5	81.30	81.30	29.57	29.57
May	132.05	132.83	20.95	20.93	10.3	10.3	81.77	82.42	29.33	29.49
June	132.77	133.62	20.85	21.09	10.6	10.6	82.23	82.91	29.69	29.62
July	132.82	134.34	20.91	20.86	10.4	10.8	82.58	83.59	29.33	29.89
August	133.73	134.18	20.68	20.79	10.8	10.6	82.89	84.16	30.16	29.23
September	134.06	133.66	20.64	20.87	10.8	10.7	83.22	84.14	30.20	28.66
October	134.40	134.70*	20.88	20.94*	10.5	10.4*	83.56	84.53*	29.96	29.23*
November	134.85	135.63	20.79	21.03	10.6	10.6	83.92	84.89	30.14	29.71
December	135.36	136.41	20.75	21.16	10.7	10.7	84.31	85.32	30.30	29.93
January 1989	135.94	136.68	21.21	21.21	10.5	10.6	84.74	85.66	29.99	29.81
February	136.44	137.53	21.03	21.37	10.6	10.7	85.12	86.14	30.29	30.02
March	136.93	138.18	21.06	21.45	10.6	10.7	85.49	86.59	30.38	30.14
April	137.56	138.31	21.38	21.58	10.5	10.6	86.09	86.85	30.09	29.98
May	138.13	138.81	21.49	21.65	10.4	10.6	86.71	87.19	29.93	29.97
June	139.11	139.11	21.57	21.76	10.5	10.5	87.33	87.62	30.21	29.73
July	139.14	139.82	21.55	21.70	10.1	10.7	87.77	87.94	29.82	30.18
August	139.78	140.35	21.57	21.68	10.2	10.7	88.20	88.43	30.01	30.34
September	140.28	140.83	21.79	21.89	10.1	10.6	88.56	88.89	29.93	30.05

Fore. = August Forecast
C.E. = Current Expectations
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CONSTRUCTION

	Housing Starts		Single Family Starts		Housing Permits		Construction Expenditures (Current)		Construction Expenditures (Real)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1988	1.584	1.584	1.093	1.093	1.449	1.449	402.7	396.2	348.2	344.3
May	1.384	1.393	0.996	1.004	1.436	1.436	407.1	398.5	350.2	345.3
June	1.454	1.465	1.098	1.092	1.489	1.493	408.5	395.7	350.6	342.8
July	1.526	1.477	1.105	1.075	1.443	1.420	408.8	398.3	350.3	343.4
August	1.481	1.431	1.073	1.068	1.392	1.464	409.0	396.1	349.9	341.7
September	1.448	1.453	1.050	1.050	1.365	1.399	408.6	401.6*	349.2	345.9*
October	1.459	1.441*	1.046	1.046*	1.372	1.386*	410.4	401.4	349.6	344.5
November	1.465	1.467	1.040	1.054	1.380	1.393	412.4	404.0	350.1	346.8
December	1.462	1.461	1.036	1.059	1.382	1.382	413.9	404.3	350.2	346.4
January 1989	1.458	1.459	1.035	1.065	1.365	1.385	414.4	405.0	349.7	345.3
February	1.450	1.459	1.040	1.062	1.350	1.371	416.8	406.1	350.8	345.3
March	1.446	1.443	1.031	1.051	1.354	1.362	418.4	407.0	351.0	345.2
April	1.440	1.435	1.026	1.029	1.343	1.343	420.2	406.4	351.6	343.5
May	1.443	1.439	1.020	1.037	1.345	1.350	420.6	406.7	351.1	342.9
June	1.437	1.431	1.014	1.028	1.350	1.344	420.3	408.1	349.7	342.9
July	1.409	1.415	1.001	1.007	1.317	1.348	422.5	408.0	350.3	342.0
August	1.402	1.389	0.996	0.995	1.296	1.316	423.9	407.0	350.3	340.3
September	1.396	1.399	0.990	0.991	1.301	1.319	425.3	407.8	350.6	339.8

	Non-Residential		Public Construction		Residential Construction	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1988	128.3	126.5	79.1	77.7	195.3	192.0
May	134.8	129.8	78.9	78.3	193.4	190.4
June	135.9	129.6	79.4	78.0	193.2	188.1
July	136.4	129.7	78.9	79.2	193.5	189.4
August	136.9	127.8	78.8	77.5	193.3	190.8
September	136.5	129.4*	78.8	79.5*	193.3	192.7*
October	137.0	129.6	79.0	79.8	194.4	192.0
November	137.4	130.3	79.2	80.3	195.8	193.4
December	137.8	130.5	79.2	80.1	196.9	193.7
January 1989	138.6	131.1	79.6	80.4	196.2	193.5
February	139.8	130.7	80.1	80.7	196.9	194.7
March	141.1	131.5	80.5	81.1	196.8	194.4
April	142.0	132.2	80.9	80.8	197.3	193.4
May	141.5	132.0	81.2	81.2	197.9	193.5
June	140.3	132.5	81.5	81.4	198.5	194.2
July	142.4	133.3	82.1	81.5	198.0	193.2
August	143.3	133.2	82.8	81.8	197.8	192.0
September	144.2	133.9	83.5	82.2	197.6	191.7

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BUSINESS ACTIVITY

	Manufacturers' Inventories		Durable Goods Orders		Non-Defense Capital Goods Orders		Non-Defense Capital Shipments	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1988	340.9	340.9	117.27	117.27	33.49	33.49	31.07	31.07
May	343.1	340.1	115.10	115.37	31.50	31.52	31.76	31.67
June	344.9	342.0	125.23	125.44	34.57	35.46	31.98	31.82
July	346.3	343.8	118.46	116.11	31.86	36.21	32.07	32.01
August	348.8	345.6	119.63	122.73	32.15	38.71	32.17	32.34
September	350.2	347.3*	120.15	117.70	32.36	34.09	32.26	31.95
October	352.9	348.8	119.11	119.23*	32.53	34.65*	32.53	32.16*
November	355.1	350.3	120.43	118.51	32.93	33.84	32.67	32.35
December	357.3	351.9	121.62	118.26	33.46	33.92	32.82	32.63
January 1989	359.5	353.6	119.85	116.94	32.55	32.84	33.02	32.45
February	361.2	355.6	120.36	117.72	32.93	33.65	33.20	32.59
March	363.0	357.2	121.45	118.84	33.14	33.98	33.38	32.85
April	365.6	358.9	121.89	119.93	33.48	34.27	33.46	33.11
May	368.1	360.9	122.53	119.52	33.65	34.15	33.55	33.26
June	370.6	363.3	122.76	120.21	33.92	34.05	33.63	33.49
July	372.3	365.5	122.50	119.46	33.98	33.63	33.70	33.62
August	374.5	367.8	121.89	119.93	33.91	33.69	33.83	33.70
September	376.8	369.7	123.26	119.65	33.84	33.48	33.96	33.74

	Business Inventories		Defense Shipments		Industrial Production		Capacity Utilization	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1988	723.7	723.7	8.47	8.47	135.4	135.4	82.6	82.7
May	728.4	725.8	8.37	8.38	136.1	136.1	82.9	82.9
June	732.0	731.5	9.07	8.72	136.6	136.5	83.1	83.0
July	736.1	735.9	8.94	8.66	137.3	138.1	83.3	83.8
August	740.3	741.7	8.63	9.02	137.0	138.3	83.0	83.8
September	744.6	744.7*	8.65	8.74	137.6	138.3	83.2	83.6
October	748.7	748.4	8.70	8.62*	138.2	138.7*	83.4	83.7*
November	753.5	752.6	8.75	8.69	138.6	139.1	83.5	83.8
December	758.1	757.0	8.75	8.76	139.0	139.7	83.7	84.0
January 1989	761.9	761.7	8.83	8.81	139.5	140.3	83.8	84.2
February	765.7	767.0	8.89	8.80	140.0	140.7	83.9	84.3
March	768.5	770.9	8.95	8.85	140.5	141.3	84.1	84.5
April	773.6	774.6	9.15	9.03	141.1	141.6	84.2	84.5
May	781.0	779.9	9.02	9.00	141.3	141.9	84.2	84.5
June	788.5	785.9	8.96	9.13	141.5	142.0	84.1	84.4
July	793.4	791.7	9.11	9.10	141.6	142.3	84.0	84.4
August	796.0	796.7	9.19	9.11	141.7	142.5	83.9	84.3
September	798.5	800.8	9.26	9.16	141.6	142.6	83.7	84.2

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PRICES

	CPI-U (seasonally adjusted)		PPI Finished Goods (seasonally adjusted)		PPI-Industrial Commodities (unadjusted)		Estimated GNP Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1988	117.2	117.2	107.0	107.0	105.6	105.6	120.1	120.5
May	117.5	117.6	107.4	107.4	106.1	106.1	120.6	121.0
June	117.9	118.0	107.8	107.8	106.5	106.5	121.0	121.4
July	118.3	118.5	108.2	108.3	106.9	106.7	121.4	121.9
August	118.8	119.0	108.7	108.9	107.3	107.1	121.8	122.2
September	119.3	119.4	109.2	109.3	106.3	106.9	122.3	122.7
October	119.7	119.8*	109.6	109.2*	107.5	107.2*	122.6	123.1
November	120.1	120.2	110.0	109.4	107.7	107.3	122.9	123.5
December	120.5	120.6	110.3	109.7	107.7	107.7	123.2	123.8
January 1989	121.0	121.2	110.8	110.3	108.3	108.3	123.7	124.2
February	121.6	121.6	111.3	110.6	108.9	108.6	124.3	124.6
March	122.0	122.0	111.6	110.9	109.5	109.0	124.9	125.1
April	122.7	122.4	112.2	111.2	110.1	109.4	125.4	125.4
May	123.4	122.9	112.8	111.5	110.7	109.8	125.8	125.9
June	124.1	123.4	113.4	111.8	111.3	110.2	126.2	126.3
July	124.6	123.8	113.8	112.2	112.0	110.7	126.7	126.8
August	125.2	124.3	114.3	112.6	112.5	111.1	127.1	127.2
September	125.8	124.7	114.8	113.0	111.6	110.6	127.5	127.8

	Consumption Deflator		Consumer Durables		Consumer Nondurables		Consumer Services		Implicit Construction Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1988	123.3	123.4	109.3	109.3	115.5	115.5	133.3	133.4	115.6	115.1
May	123.9	124.0	109.4	109.5	116.1	116.2	133.8	134.1	116.2	115.4
June	124.2	124.3	109.9	109.9	116.4	116.3	134.3	134.5	116.5	115.4
July	124.7	124.8	110.1	110.1	116.8	116.9	134.8	135.1	116.7	116.0
August	125.1	125.1	110.3	110.4	117.1	117.1	135.4	135.5	116.9	115.9
September	125.5	125.8	110.4	110.6	117.4	117.9	136.0	136.1	117.0	116.1*
October	126.0	126.2*	110.9	110.8*	117.9	118.4*	136.5	136.6*	117.4	116.5
November	126.5	126.7	111.2	111.3	118.4	118.8	136.9	137.2	117.8	116.7
December	127.0	127.1	111.5	111.6	118.8	119.1	137.3	137.7	118.2	117.0
January 1989	127.5	127.8	111.7	111.8	119.5	119.5	138.1	138.2	118.5	117.3
February	128.1	128.2	111.9	112.1	120.0	120.0	138.8	138.8	118.8	117.6
March	128.7	128.6	112.1	112.3	120.5	120.5	139.5	139.4	119.2	117.9
April	129.4	129.0	112.4	112.6	121.4	120.8	140.1	140.0	119.5	118.3
May	130.1	129.5	112.7	112.8	122.5	121.2	140.7	140.6	119.8	118.6
June	130.8	130.1	113.0	113.0	123.6	121.8	141.3	141.1	120.2	119.0
July	131.3	130.6	113.3	113.3	123.8	122.4	142.0	141.7	120.6	119.3
August	131.8	131.2	113.6	113.6	124.0	122.9	142.7	142.3	121.0	119.6
September	132.4	131.7	113.9	113.8	124.2	123.5	143.4	142.9	121.3	120.0

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MISCELLANEOUS

	Merchandise Trade Balance		Leading Indicators		Estimated GNP		Estimated GNP (1982 $)		IVA (annual rate)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1988	-10.27	-8.51	192.8	192.5	4778	4783	3979	3969	-18.3	-23.3
May	-10.93	-8.88	192.6	191.1	4806	4826	3985	3988	-19.6	-28.4
June	-10.10	-11.06	194.9	193.7	4830	4860	3995	4003	-29.1	-30.5
July	-10.76	-10.48	194.0	192.7	4869	4888	4011	4010	-26.2	-27.2
August	-10.59	-11.12	194.5	193.4	4885	4900	4011	4010	-23.0	-23.7
September	-10.42	-10.14*	195.3	193.6*	4908	4915	4013	4006	-20.1	-18.5
October	-10.36	-9.73	194.7	194.2	4934	4943	4024	4015	-20.0	-13.4
November	-10.30	-9.46	194.0	194.5	4965	4976	4040	4029	-18.6	-11.6
December	-10.24	-9.27	193.8	193.7	4997	5005	4056	4043	-18.3	-12.9
January 1989	-9.56	-8.83	193.9	194.0	5034	5038	4070	4056	-19.7	-14.4
February	-9.27	-9.28	192.6	194.4	5065	5070	4075	4069	-21.2	-14.8
March	-8.86	-9.42	192.5	194.0	5097	5098	4081	4075	-22.8	-12.3
April	-8.96	-8.93	193.1	193.5	5128	5123	4089	4085	-27.3	-11.6
May	-8.94	-8.98	193.6	193.1	5159	5161	4101	4099	-30.5	-10.9
June	-8.90	-8.51	193.0	193.5	5189	5193	4112	4112	-33.1	-14.6
July	-8.98	-8.86	192.5	193.8	5220	5216	4120	4114	-31.5	-16.3
August	-9.15	-9.13	192.9	193.2	5241	5237	4124	4117	-30.0	-20.1
September	-8.92	-8.85	192.7	192.7	5262	5262	4127	4117	-28.5	-22.4

	Currency Index		Adjusted Profits		30-Year Government Bonds		New York Composite	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1988	88.95	88.95	181.4	180.4	8.95	8.95	148.46	148.46
May	89.74	89.74	180.9	180.9	9.23	9.23	144.99	144.99
June	92.58	92.58	182.5	188.3	9.00	9.00	152.72	152.72
July	95.65	96.53	176.5	191.2	9.23	9.14	150.65	152.12
August	96.20	98.29	170.4	188.5	9.25	9.32	151.93	149.25
September	96.86	97.91	169.3	183.7	9.11	9.06	153.24	151.47
October	93.27	94.43*	170.5	184.8	9.22	8.92*	153.06	156.24*
November	89.42	90.28	173.3	188.2	9.53	8.73	151.47	161.58
December	92.41	88.35	176.2	193.1	9.86	8.68	150.16	165.77
January 1989	93.12	90.26	175.0	196.7	10.04	8.78	149.23	165.95
February	93.76	88.53	172.9	200.4	10.16	8.83	147.65	167.16
March	93.62	90.22	170.8	203.5	10.31	8.80	146.16	169.40
April	93.74	87.71	169.5	200.6	10.50	8.79	142.29	168.11
May	93.91	89.43	169.0	196.5	10.43	8.96	139.63	162.39
June	93.75	91.26	170.3	194.1	10.59	9.28	139.98	155.74
July	94.83	91.55	171.5	194.0	10.65	9.53	140.42	152.52
August	96.27	93.62	171.1	192.3	10.61	9.67	143.57	148.97
September	93.60	93.21	171.9	188.7	10.52	9.65	146.71	147.47

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FINANCIAL MARKETS

	Monetary Base		M1		M2		Federal Funds		T-Bills (6 Mos.)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1988	275.8	275.7	770.2	770.1	2991.9	2990.9	6.87	6.87	6.21	6.21
May	276.7	276.2	770.1	770.2	3003.7	3002.2	7.09	7.09	6.56	6.56
June	277.8	278.9	776.4	776.5	3018.1	3016.5	7.51	7.51	6.71	6.71
July	280.3	280.3	783.5	782.4	3028.9	3025.9	7.64	7.75	7.05	6.99
August	282.3	281.1	789.6	782.5	3043.5	3031.8	7.81	8.01	7.16	7.36
September	284.4	282.1	795.5	782.5	3058.2	3035.1	7.96	8.19	7.27	7.43
October	286.0	282.5*	799.4	784.3*	3076.3	3040.5*	8.10	8.25*	7.36	7.47*
November	287.2	283.5	802.6	787.3	3094.0	3058.7	8.16	8.22	7.42	7.43
December	288.4	284.6	803.7	790.9	3112.5	3080.1	8.22	8.18	7.48	7.40
January 1989	290.3	286.0	808.5	795.9	3133.4	3101.7	8.20	8.29	7.40	7.48
February	292.5	287.4	814.9	800.4	3151.2	3123.4	8.23	8.35	7.35	7.56
March	294.6	288.9	821.3	804.6	3169.4	3142.1	8.26	8.32	7.36	7.55
April	296.3	290.0	824.6	807.1	3185.2	3157.8	8.53	8.47	7.64	7.69
May	297.6	291.3	827.0	810.4	3207.2	3176.7	8.86	8.63	8.03	7.85
June	298.9	292.4	829.5	812.9	3228.9	3192.6	9.19	8.75	8.30	7.94
July	300.5	293.5	835.1	815.3	3246.5	3205.4	9.25	8.79	8.20	8.03
August	302.7	294.9	840.0	818.9	3262.7	3221.6	9.11	8.83	7.92	8.17
September	304.9	296.0	844.8	821.4	3278.8	3237.7	9.05	8.89	7.63	8.20

	Aaa (Seasoned)		Municipals (Bond Buyer)		(3 Month) Commercial Paper		90 Day CD's		Prime Rate	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1988	9.67	9.67	7.81	7.81	6.86	6.86	6.92	6.92	8.50	8.50
May	9.90	9.90	7.91	7.91	7.19	7.19	7.24	7.24	8.84	8.84
June	9.86	9.86	7.78	7.78	7.49	7.49	7.51	7.51	9.00	9.00
July	10.02	9.96	7.88	7.76	7.73	7.82	7.86	7.94	9.42	9.29
August	10.08	10.11	7.93	7.79	7.92	8.26	8.03	8.35	9.50	9.84
September	10.15	9.82	7.96	7.66	8.05	8.17	8.14	8.23	9.50	10.00
October	10.20	9.59*	8.01	7.52*	8.15	8.22*	8.26	8.32*	9.56	10.00*
November	10.23	9.74	8.00	7.50	8.22	8.16	8.35	8.25	10.00	10.00
December	10.26	9.70	8.03	7.45	8.30	8.12	8.39	8.19	10.00	10.00
January 1989	10.39	9.85	8.15	7.59	8.30	8.33	8.43	8.41	10.00	10.00
February	10.46	9.92	8.20	7.68	8.34	8.36	8.45	8.50	10.00	10.22
March	10.50	9.86	8.23	7.62	8.40	8.31	8.51	8.46	10.00	10.25
April	10.78	9.78	8.42	7.45	8.59	8.52	8.62	8.59	10.00	10.25
May	10.93	9.94	8.59	7.65	8.82	8.65	8.93	8.76	10.46	10.53
June	11.10	10.15	8.66	7.88	9.15	8.68	9.23	8.81	10.95	10.75
July	11.01	10.42	8.57	8.11	9.26	8.84	9.30	8.93	11.00	10.75
August	10.90	10.55	8.43	8.24	9.10	8.90	9.16	9.02	10.87	10.75
September	10.78	10.51	8.35	8.20	8.98	8.95	9.05	9.11	10.50	10.75

Fore. = August Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

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MONTHLY PROJECTIONS
November 1988

Dr. Donald Ratajczak, Director
For Release: December 14, 1988

ELECTIONS, GORBACHEV AND OPEC ALL BUFFET ECONOMY

Two elections, in the United States and Canada, OPEC's off-again, on-again oil production and pricing agreements, and Mikhail Gorbachev's unilateral withdrawal initiative in Eastern Europe all impacted the economy in the past month. When all the factors were considered, the results were not appreciably different from before all these events took place. However, inflationary pressures early in 1989 probably will be higher than originally anticipated while currency values and long-term interest rates, seeking promises from the peace initiative, may be lower than previously expected.

Although events may change dramatically after president-elect George Bush assembles his total cabinet, the early appointments, which include virtually all his economic team, suggest no dramatic changes in policy. Dr. Michael Boskin created the "flexible freeze" to demonstrate how growth may eliminate budget deficits, a concept that George Bush himself denied when he was running against President Reagan eight years ago. The other appointments, from Brady to Hills suggest continuity without drama. Apparently, President Bush, like President Reagan before him, will try to wait out the consequences of structural federal deficits.

In the meantime, the Congress has a guideline of its own in the Gramm-Rudman legislation that will require $48 billion in reductions in the fiscal year beginning next October. With President Bush refusing, at this time, to consider any significant revenue initiatives, these deficit reduction targets almost certainly are unachievable. Dan Rostenkowski's initiative to increase taxation of social security benefits while raising gasoline taxes provides a means of closing the gap between deficit targets and reality, but the administration-in-waiting has indicated no inclination to follow such a proposal. When foreign investors became aware that continuity rather than new directions was likely from the new administration, they decided that the American dollar was a poor place to put their liquid assets. As a result, the dollar fell dramatically late in November and early in December.

Then the Soviet president came to New York bearing unilateral defense gifts from the East. Not only did the Soviet president indicate that he would reduce tank divisions in Europe and other parts of the Soviet sphere but he also suggested that remaining troops in East Europe would take a defensive posture. In effect, he declared that the Soviet mission no longer was one of spreading the revolution but rather was one of raising the economic well-being of the Soviet people, which was falling dramatically behind countries in Asia and Europe. Of course, an announcement by a Soviet leader is not sufficient to insure success. The military industrial complex in Russia is even more powerful than it ever attained in the United States. Nevertheless, the peace overture is a major departure in Soviet policy that provides opportunities for reducing conventional forces in the NATO alliance.

The long-run implications of Mr. Gorbachev's initiative can be significant. Indeed, if these proposals are carried out, the United States may be able to reduce its defense spending over time by more than 20% as a share of GNP. However, even the Soviet Union will not be able to achieve its objectives until 1991. Any U.S. response clearly will need to be delayed until after the new administration has assembled its defense and security teams. Nevertheless, the new peace environment holds opportunities for reducing defense spending in the next budget. The Bush administration reportedly already was seeking more than $10 billion of reductions from President Reagan's defense proposals to be released January 9. Another $5 to $10 billion of reductions possibly could be added in response to the Soviet initiative.

While reduced defense spending could significantly reduce the structural deficit, substantial savings probably are not likely until the third and fourth years of the Bush administration. Nevertheless, the changed climate indicates that President Bush's budgetary restraint augmented by accelerated defense spending reductions could achieve a structural balance in the budget before the end of his first term.

Such an outcome has excited the fixed-income markets. Interest rates on long-term government bonds have increased nearly 30 basis points since Gorbachev's U.N. speech. Moreover, this improved prospect for reducing the savings deficiency in the United States has stayed the hand of foreign investors. However, these investors will not wait very long to see a response to the Soviet initiative from the United States. Therefore, the dollar is expected to begin falling again before the end of this year and early in the new year.

The Canadian elections were a modest shot-in-the-arm for free trade. Once again, the lead times in gaining efficiencies through reduced regulations and restraints across the U.S. and Canadian borders will take up to ten years. Moreover, the Canadians probably will garner more benefits from having freer access to the American markets than will be achieved in the other direction because of the relative sizes of the two economies. Nevertheless, increased efficiencies probably will reduce cost pressures by slightly less than a percentage point in the United States and by several percentage points in Canada. These gains pale in comparison to the more than 6-percentage-point reduction in production costs that can be achieved through an integrated European economy according to some studies. Thus, the relative competitiveness of the United States does not improve when the two initiatives are put together. However, the European free trade zone is not yet a reality.

Finally, the OPEC nations, as expected, agreed to production restraints that would gradually firm oil prices. Indeed, current production targets of 18.5 million barrels a day from the OPEC nations is probably 2 million barrels less than currently is needed during the heating season. However, substantial excess inventory of oil product exists in the world today. Moreover, the 18.5 million quota will not be sufficient to preserve prices during the spring and early summer months. Furthermore, substantial cheating has greeted previous production quotas after only a few months. There is no reason to assume that any other result should develop from the current agreement.

Thus, the net effect of the OPEC agreement is to raise our estimates of inflation over the next three months as a result of higher energy prices but to bring those prices down in the spring. The longer-term inflationary implications are not expected to be substantial.

When all the effects are summed, slightly lower interest rates along with slightly higher near-term inflation appear to be developing. The higher inflation may require more significant Federal Reserve restraint than currently is contemplated. If so, short-term interest rates could rise above long-term interest rates over the next few months. Such an inverted yield curve is an aberration. However, the liquidity restraints associated with such a yield structure normally lead to substantial inventory reductions followed by a slowing in interest-sensitive sectors of the economy. In short, a movement toward recessionary behavior could be spawned by any serious interest rate inversion. Such an outlook of recession is not currently anticipated for 1989, although further Federal Reserve tightening later in 1989 could lead to a moderate recession in 1990.

Quarterly Profile of GNP

	1988-3	1988-4	1989-1	1989-2	1989-3	1989-4	1988 Annual	1989 Annual
Real:	2.6	1.9	4.9	2.6	2.0	1.3	3.9	2.9
Price:	4.7	4.3	4.3	4.2	4.8	4.8	3.3	4.5
Nominal:	7.3	6.3	9.3	6.9	6.9	6.2	7.3	7.5

Monthly Statistical Highlights for November 1988

(NOTE: For production reasons, the timing of this report will be changed to be released the week after the monthly employment report. As a result, the statistical highlights will be for all monthly data following those already released from the payroll situation.)

Personal income +0.1%; savings rate 4.6%; personal consumption +0.8%; retail sales +0.9%; auto sales 10.1 million units; housing starts -3.8%; housing permits -4.5%; construction expenditures +0.7%; business inventories +0.5%; orders for durable goods -1.2%; orders for non-defense capital goods +2.4%; industrial production +0.4%; CPI +0.4%; PPI +0.4%; consumption deflator +0.3%; leading indicators -0.2%; currency index -3.4%; equity index -2.4%; real GNP(AR) +2.1%; M1(AR) +1.1%; M2(AR) +6.6%.

Monthly Statistical Highlights for December 1988

Payroll employment +203,000; index of hours worked +0.2%; household employment +218,000; civilian unemployment rate 5.3%; personal income +0.5%; savings rate 4.4%; personal consumption +0.7%; retail sales +0.8%; auto sales 10.4 million units; housing starts -0.2%; housing permits -0.3%; construction expenditures -0.1%; business inventories +0.5%; orders for durable goods +0.3%; orders for non-defense capital goods +0.5%; industrial production +0.4%; CPI +0.4%; PPI +0.4%; consumption deflator +0.4%; leading indicators +0.2%; currency index -1.6%; equity index +2.2%; real GNP(AR) +1.2%; M1(AR) +5.3%; M2(AR) +7.4%.

Commentary

Employment - Although a 463,000 spurt in payroll employment during November clearly was far in excess of anticipations, a substantial portion of that gain was offset by reduced weekly hours worked in the private economy. The index of hours worked declined slightly in November. Therefore, strength that otherwise would have been indicated by such a large employment gain was largely dissipated. Moreover, the hourly earnings index remained unchanged in November following an unexpectedly brisk rate of increase in October. Thus, fears that the labor markets were getting too tight have diminished slightly. Also, the civilian unemployment rate rose slightly.

Nevertheless, employment was strong in the manufacturing sector and the workweek did not decline there. This indicates that the goods-producing sector of the economy remained strong in November. Furthermore, construction employment and hours also rose. Favorable weather may have been responsible for more construction activity than seasonally occurs in the month of November. Thus, some declines in the construction component certainly are expected for December. On the other hand, retail employment remained sluggish as retailers continued to be cautious about their Christmas prospects.

Productivity in the nonfarm economy rebounded during the third quarter, suggesting that weak labor market demand ahead is no longer likely. Of course, compensation also accelerated. Indeed, many analysts are increasingly concerned by the more than 5% annualized return on compensation during the summer months. Compensation is expected to slow slightly during the fall and winter months. Indeed, our estimates are for an average of 5.5% for all of 1989. Nevertheless, if compensation continues to intensify, higher unit labor costs and higher inflation than currently anticipated will develop.

Personal Income - Personal income surged in October as a result of a significant increase in farm subsidies and a 1.5% contribution from wages and salaries. The surge in wages and salaries clearly reflected the strong employment gains in October along with a one-time bonus to auto workers. However, reduced wage gains suggest that wage and salary growth in November will be modest. Some gains are anticipated in property income, but personal income probably will show minimal growth in November. More normal growth both in wages and salaries and in personal income are expected in December.

Because of the surge in wages and farm subsidies in October, the savings rate surged above 5%. Obviously, this is a level from which relatively strong consumer spending can develop during the Christmas season.

Sluggishness in auto sales early in the new model year suggested that consumer spending may have been slowing. However, a delay in offering new cars by Chrysler and Ford could be distorting the seasonals. In addition, the new W cars provided by GM started slowly but began increasing acceptably in November. If these cars now attain acceptable levels, auto sales could be stronger in the next few months than previously anticipated. Exceptionally strong auto sales after seasonal adjustment may develop early in the new year as Ford and Chrysler models become available.

In the meantime, consumers reacted to their increased incomes. Retail sales in October rose a sharp 0.9% and should rise a further sharp percentage in November. Growth did not develop for other hard goods in October, but they are expected to improve later in the Christmas season.

A surge in service expenditures in October occurred following a slowing in September as a result of the ending of a heat wave. Unusually mild weather could lead to less than normal expenditures growth for services in November before more normal growth rates return in December. Of course, this will allow greater purchasing power for consumers to buy automobiles and other retail goods in the Christmas season.

Construction - Normally, rising interest rates would begin restricting housing starts at this time. However, a surprising spurt in starts and in permits during October raised questions about the current direction of housing activity. In addition, the employment report showed that weather may have been milder than normal in November, leading to surprising spurts in construction activity. Our current projections are for a modest slowing in housing activity as interest rates gently rise. However, strength in the housing markets on the West Coast could persist into the first half of 1989. Under such conditions, stronger housing activity could develop. Of course, with the consumer, industrial activity, and housing all trying to grow late in 1988 and early in 1989, the economy will become overheated and higher interest rates will result. This is not contained in our forecast but certainly is a significant risk that must be considered.

Excluding the spurt in housing activity, other construction activity continues to move sideways. Public construction showed some strength, but this may be the result of favorable weather conditions following disrruptions caused by the summer heat wave. Nonresidential construction continues to sag modestly. Significant vacancy rates should continue to create slight downward pressures upon nonresidential activity through next year.

The construction cost index shows only modest increases as both construction employment and construction materials are showing well-behaved price patterns at the present time. Substantial numbers of construction contracts are up for renegotiation early in 1989. However, sluggishness in the construction industry probably will prevent any serious acceleration of wage pressures at that time.

Business Activity - Manufacturers are beginning to accelerate their pace of inventory accumulations. This is the result of modest increases in sales and should persist through the first half of 1989. Wholesalers also are increasing their inventory holdings while retailers early in the fall held higher than desired inventories. Rising retail sales, however, should remove any glut by the end of the fall.

Large increases in defense orders once again distorted orders for durable goods in October. These orders probably will reverse themselves in November causing some dip in overall durable goods activity. Some large commercial aircraft orders have not yet been recorded in the government statistics. As a result, these orders will strengthen nondefense capital goods orders in the next few months. The traditional January falloff in machinery orders is anticipated despite a lessening of tax advantages that previously caused the seasonal aberration in ordering activity.

Defense shipments are expected to grow gradually in the second half of 1989 as weapons systems that had been developed under President Reagan get into full production. Thus, the peace initiative should not have a significant impact upon actual defense shipments until beyond 1989.

Industrial production is expected to continue rebounding in November with activity especially strong in the business equipment area. Some strength also is expected for consumer goods and industrial materials. Capacity utilization should gradually grow to more than 85% in the second half of 1989. While cyclical peaks do not normally end at this level of utilization, inflationary pressures certainly will be building.

Prices - Although the OPEC agreement is expected to last only a few months before significant cheating forces prices down again, the timing of this agreement is favorable for strengthening prices through the heating season. As a result, our price estimates have been increased early in 1989. In addition, several raw material prices once again are beginning to intensify as a result of the reacceleration of the industrial sector. Indeed, sensitive prices measured by the Journal of Commerce have increased nearly 3% in the past three weeks. Our November survey of sensitive prices for the PPI did not show this acceleration, but the December price increases probably will. Therefore, some intensifying inflationary pressures are being generated. We still believe that moderate Federal Reserve restraint that has been in place for several months will begin slowing the economy early in 1989. As a result, inflationary pressures are not expected to grow dramatically. In addition, declines in oil prices in the spring should provide another respite from rising inflationary pressures. Nevertheless, prices will be rising nearly 5% as measured by the CPI over the next twelve months and by nearly 4.5% as measured by the Producer Price Index.

Obviously, these greater inflationary pressures lead to increased estimates of the GNP deflator. It is noteworthy, however, that only a small percentage of these price increases will be reflected in rising consumer prices.

Miscellaneous - The dollar's strength earlier this year is having an adverse effect upon export growth. As a result, merchandise trade balances probably will not show any further improvement until the second half of next year. Rising oil prices also impart adverse conditions upon the trade balances. However, once the dollar again weakens in the second half of next year, as reflected in our currency index, our trade balances will gradually improve. More significant substitution away from imports also is anticipated. Therefore, previous conclusions that the trade balances will flatten near $10 billion do not appear to be confirmed by our own analysis, which continues to show improved trade balances as a response to weakening dollar values.

Adjusted profits were not as high as originally thought for the summer months. However, strong growth in the nonfarm economy should lead to higher profit growth in the winter than had been projected. Slowing in the economy in the second half of next year along with rising interest rates and upward pressures on wages will eventually slow corporate profitability adjusted for inflation and tax payments.

As a result of that downward trend in profitability, stock market values are not expected to significantly exceed current levels. A slight rebound in stock market values is possible in late winter and early spring as oil prices ease and interest rates momentarily decline. However, significant downward trends in equity values are anticipated in the second half of 1989, at least until interest rates begin falling in earnest at the end of that year.

Financial Markets

Whether reductions in government deficits will be generated in the future as a result of the current peace initiative, deficits for the next fiscal year will be hard-pressed to reach the $100 billion required by Gramm-Rudman legislation. With receipts partially indexed for inflation and benefits also adjusted upward as inflation intensifies, inflation no longer is a substantial tax collector for the federal government. Indeed, rising interest rates increase expenditures almost as rapidly as revenues are growing. Moreover, the current corporate restructuring may begin to have a significant impact upon corporate tax collections. Many of the LBOs are at least partially financed out of the tax savings that are generated in order to pay the interest necessary to buy out the shares. The latest proposal to unbundle equity values contained in current stocks increases the raid on government revenues. In the absence of significant adjustments to taxable interest rate deductions, falling corporate tax receipts soon will develop.

Thus far, corporate restructurings have not gone far enough to significantly alter budget projections. However, the reduced growth that is expected in 1989 will slow receipts to only slightly more than the growth in expenditures in the absence of significant revenue raisers. Thus, the government deficit probably will fall next fiscal year, but only to the vicinity of $140 billion. This will be significantly less than required to meet Gramm-Rudman targets.

Moreover, these deficit estimates do not include borrowings by bank agencies in order to resolve problems in the thrift industry. More than $20 billion probably will be issued to restructure thrift assets in 1989. More than $50 billion probably will be needed before all poorly managed assets are recycled to alternative management oversight. Thus, total government borrowings probably will rise next year, contributing to upward pressures upon interest rates.

In the household sector, housing purchases probably will diminish as interest rates continue rising. Installment credit growth probably will slow to less than the growth of income. This could result in a modest increase in the savings rate. However, the savings rate rose sharply as a result of special wage transfers in October. Such transfers will not be as significant later in the year. For that reason, the savings rate will only gradually drift upward to slightly more than 5% in 1989. Nevertheless, the household sector will largely be exerting downward pressures upon interest rates as they increase their savings.

Corporate restructuring will reduce the degree of savings generated in the corporate sector. Unlike Japan, where households are the primary accumulator of savings, accumulated retained earnings provide a major contribution to gross savings in the United States. Indeed, many corporate capital spending programs are self-financed. However, the conversion from equity to interest payments will significantly reduce the equity ownership in corporations. While the transfer of assets is neutral, interest recipients probably are more prone to consume their accumulated earnings than equity owners. Thus, corporate restructuring probably is leading to a secular decline in the corporate savings being generated.

Next year, corporate borrowings for inventory purposes also will be leading to reduced corporate savings. High returns on commercial paper already reflect significant corporate borrowings. While corporate profitability may improve corporate cash flow early in 1989, profit deterioration will require increased borrowings later in the year. The normal lag between reductions in cash flow and reductions in investment spending should lead to significant liquidity borrowing by the corporate sector in the second half of the year.

Excluding the savings desires of foreign investors, this brief flow of funds analysis suggests that interest rates will remain high early in the year and resume rising in the second half.

Foreign investors momentarily may be encouraged by potential reductions in government borrowings. As a result, moderate interest rate pressures should have only marginal impact upon increasing interest rates during the first half of next year. In the second half, however, pressures should be intensifying. Therefore, interest rates probably will rise more vigorously later in the year after a pause in the first part of this year. Moreover, the Federal Reserve probably will reinforce increased interest rate pressures by attempting to restrain economic activity as inflation intensifies. The yield curve could actually invert even at the shortest level. (The interest rate curve already is slightly inverted from one year to thirty years in maturity.)

Equity Markets - For the next several months, rising corporate profits and relatively stable interest rates should provide favorable conditions for equity values. Indeed, the Dow Jones probably could rise an additional 10% to more than 2300 by the spring. Later in the year, however, rising interest rates and reduced corporate profitability as wages intensify should once again place downward pressures upon equity values. Thus, the stock market should trend downward in the second half of the year. Although rising interest rates do not usually provide opportunities for interest-sensitive investments, increased corporate borrowings may aid the earnings of regional banks while the significant cash flow of many utilities could increase their attractiveness. Some of the multinationals should again perform well as the dollar eases in the first half of next year. Chemicals, fabricated metals, nonelectrical machinery, and commercial aircraft companies still are expected to outperform the market during the next six months. However, some other industries, such as plastics, rubber, paper, and textiles no longer show capacity pressures that helped them improve their profit margins earlier in the year. For that reason, no significant improvement is expected in that group.

While the consensus forecast seems to be that inflationary pressures and interest rates will intensify early in 1989 and equity values will be under downward pressure, our outlook shows a different pattern. When OPEC pricing falls apart, inflation should momentarily ease in the spring. Interest rates should decrease slightly. Then, higher inflationary pressures as a result of intensifying wage pressures along with the impact of a falling dollar will add to the inflation risk. Interest rates then will rise in the second half of 1989 and equity values should trend downward.

EMPLOYMENT

	Payroll Employment		Index of Hours Worked		Household Civilian Employment		Civilian Unemployment Rate		Hourly Earnings Index	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	106271	106271	126.4	126.4	115059	115059	5.4	5.4	179.3	179.3
August	106440	106425	125.5	125.5	115180	115180	5.6	5.6	179.6	179.5
September	106695	106737	126.0	126.0	115328	115328	5.4	5.4	180.4	180.3
October	106895	106975	126.3	127.1	115587	115521	5.3	5.3	181.0	181.5
November	107144	107438	126.7	127.0	115895	115976	5.2	5.4	181.5	181.5
December	107393	107641*	127.1	127.3*	116207	116194*	5.2	5.3*	182.1	182.2*
January 1989	107608	107863	127.4	127.5	116443	116405	5.1	5.3	182.8	182.9
February	107840	108059	127.7	127.7	116666	116681	5.0	5.2	183.5	183.6
March	108072	108265	127.9	127.9	116889	116910	5.0	5.2	184.3	184.3
April	108246	108492	128.1	128.2	117003	117155	5.0	5.1	184.9	184.9
May	108419	108713	128.4	128.4	117219	117416	4.9	5.0	185.4	185.5
June	108592	108924	128.5	128.6	117435	117632	5.0	5.0	186.0	186.1
July	108756	109111	128.7	128.7	117568	117875	4.9	4.9	186.7	186.7
August	108913	109317	128.9	129.0	117723	118109	4.9	4.9	187.4	187.4
September	109070	109502	129.1	129.2	117884	118313	4.8	4.9	188.2	188.1
October	109216	109685	129.2	129.4	118005	118493	4.8	4.9	188.9	188.9
November	109352	109862	129.3	129.5	118229	118655	4.9	5.0	189.5	189.6
December	109488	110009	129.2	129.6	118445	118821	4.9	5.0	190.2	190.3

PERSONAL INCOME

	Personal Income		Wage & Salary		Personal Savings		Disposable Income		Personal Outlays	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	4.071	4.074	2.452	2.452	141.0	150.1	3.487	3.489	3.346	3.339
August	4.083	4.091	2.457	2.459	132.4	132.4	3.497	3.505	3.365	3.372
September	4.103	4.113	2.471	2.473	147.5	148.3	3.513	3.524	3.366	3.376
October	4.133	4.185	2.484	2.511	148.0	188.3	3.535	3.590	3.387	3.401
November	4.158	4.190*	2.500	2.510*	152.0	165.2*	3.557	3.592*	3.405	3.427*
December	4.182	4.213	2.516	2.528	157.2	159.2	3.579	3.610	3.422	3.451
January 1989	4.204	4.230	2.535	2.543	173.4	160.0	3.612	3.630	3.439	3.470
February	4.238	4.254	2.550	2.559	168.1	167.0	3.630	3.655	3.462	3.488
March	4.270	4.277	2.565	2.574	163.0	176.2	3.645	3.677	3.482	3.501
April	4.286	4.302	2.580	2.590	159.2	183.2	3.661	3.698	3.502	3.515
May	4.300	4.323	2.592	2.603	157.4	186.4	3.678	3.716	3.521	3.530
June	4.314	4.347	2.604	2.617	155.5	199.0	3.695	3.738	3.540	3.539
July	4.340	4.367	2.619	2.628	152.3	198.4	3.711	3.754	3.559	3.556
August	4.365	4.394	2.634	2.646	149.2	200.3	3.725	3.777	3.576	3.577
September	4.390	4.416	2.649	2.661	146.3	202.1	3.739	3.795	3.593	3.593
October	4.408	4.444	2.660	2.678	146.9	206.2	3.756	3.818	3.609	3.612
November	4.429	4.466	2.673	2.691	148.5	208.3	3.778	3.836	3.630	3.628
December	4.450	4.488	2.687	2.705	145.1	211.2	3.797	3.854	3.652	3.643

Fore. = November Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

CONSUMPTION

	Personal Consumption		Durables		Nondurables		Services		Consumption Real	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	3245.3	3238.9	454.4	448.5	1053.0	1053.0	1737.9	1737.4	2600.1	2594.8
August	3263.4	3271.1	454.8	455.5	1059.6	1064.4	1749.0	1751.2	2608.1	2615.1
September	3264.1	3274.5	451.7	451.5	1060.0	1068.4	1752.4	1754.6	2595.8	2603.7
October	3283.7	3299.7	454.3	446.0	1065.6	1074.8	1763.8	1778.9	2601.1	2611.6
November	3301.3	3324.8*	457.2	458.5*	1067.9	1081.0*	1776.2	1785.3*	2607.4	2623.3*
December	3319.0	3348.3	455.3	464.4	1070.3	1087.2	1793.4	1796.7	2613.6	2632.6
January 1989	3338.3	3367.2	460.1	466.9	1073.5	1091.8	1804.7	1808.5	2620.5	2637.8
February	3356.5	3384.8	463.7	470.4	1077.4	1095.1	1815.4	1819.3	2623.9	2642.0
March	3374.2	3397.3	467.0	469.6	1081.9	1097.2	1825.3	1830.5	2627.3	2642.2
April	3401.3	3411.1	469.9	467.0	1088.5	1100.5	1842.9	1843.6	2635.9	2642.6
May	3423.6	3425.7	473.4	466.3	1097.7	1104.9	1852.5	1854.5	2537.2	2644.7
June	3421.0	3434.9	459.8	462.1	1106.8	1111.9	1854.4	1860.9	2630.8	2641.0
July	3447.5	3451.3	465.6	463.7	1112.4	1116.8	1869.5	1870.8	2637.5	2643.4
August	3468.8	3472.2	470.4	466.7	1113.1	1122.0	1885.3	1883.5	2646.2	2648.8
September	3489.9	3488.1	475.1	467.1	1114.0	1124.8	1900.8	1896.2	2655.0	2649.6
October	3506.2	3506.7	473.4	466.0	1120.6	1131.3	1912.2	1909.4	2653.2	2652.2
November	3520.7	3522.2	470.2	463.2	1129.1	1138.4	1921.4	1920.6	2654.4	2652.6
December	3534.9	3536.8	470.1	462.0	1137.7	1143.3	1927.1	1931.5	2655.7	2651.4

RETAIL SALES

	Retail Sales		Non-Auto Durables		Auto (Million Units)		Nondurable Sales		Auto Sales	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	134.34	134.34	20.86	20.86	10.8	10.8	83.59	83.59	29.89	29.89
August	134.18	134.76	20.79	20.87	10.6	10.6	84.16	84.50	29.23	29.39
September	133.66	134.38	20.87	20.83	10.7	10.5	84.14	84.80	28.66	28.75
October	134.40	135.62	20.79	20.79	10.2	9.8	84.59	85.60	29.03	29.24
November	135.10	136.87*	20.67	20.88*	10.5	10.1	84.77	85.93*	29.66	30.06*
December	135.64	138.02	20.85	20.93	10.7	10.4*	84.96	86.42	29.83	30.67
January 1989	136.06	138.67	20.91	20.95	10.7	10.6	85.21	86.79	29.94	30.93
February	136.57	139.32	20.92	21.10	10.8	10.7	85.52	87.05	30.13	31.17
March	137.09	139.40	21.16	21.23	10.7	10.6	85.88	87.22	30.05	30.95
April	137.83	139.37	21.21	21.20	10.7	10.5	86.40	87.48	30.22	30.69
May	138.84	139.64	21.38	21.16	10.7	10.5	87.13	87.83	30.33	30.65
June	138.66	139.73	20.86	21.25	10.5	10.3	87.85	88.39	29.95	30.09
July	139.35	140.30	20.97	21.28	10.5	10.4	88.30	88.78	30.08	30.24
August	139.53	141.04	21.23	21.36	10.3	10.5	88.35	89.19	29.95	30.49
September	139.69	141.31	21.46	21.33	10.2	10.5	88.43	89.41	29.80	30.57
October	140.86	141.71	21.35	21.30	10.2	10.2	88.95	89.93	30.56	30.48
November	141.18	141.09	21.10	21.25	10.1	10.0	89.62	90.49	30.46	30.22
December	142.15	142.21	20.99	21.26	10.3	9.9	90.31	90.88	30.85	30.07

Fore. = November Forecast
C.E. = Current Expectations
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CONSTRUCTION

	Housing Starts		Single Family Starts		Housing Permits		Construction Expenditures (Current)		Construction Expenditures (Real)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	1.477	1.477	1.075	1.068	1.420	1.420	398.3	401.8	343.4	346.4
August	1.431	1.461	1.068	1.078	1.464	1.464	396.1	402.8	341.7	347.6
September	1.453	1.449	1.050	1.042	1.399	1.394	401.6	405.5	345.9	349.6
October	1.465	1.554	1.067	1.146	1.413	1.497	399.2	409.2	343.3	352.2
November	1.430	1.495*	1.052	1.080*	1.378	1.430*	397.4	412.0*	341.1	353.9*
December	1.433	1.492	1.043	1.083	1.385	1.425	395.6	411.5	339.0	352.9
January 1989	1.442	1.459	1.056	1.052	1.372	1.416	398.9	407.5	341.5	348.6
February	1.435	1.428	1.071	1.027	1.359	1.401	401.3	405.8	343.0	346.5
March	1.463	1.420	1.062	1.034	1.384	1.377	403.8	402.6	344.5	343.2
April	1.439	1.425	1.045	1.037	1.359	1.380	403.8	403.3	344.0	343.2
May	1.442	1.443	1.036	1.053	1.365	1.402	403.4	404.5	343.6	343.7
June	1.426	1.416	1.030	1.022	1.329	1.375	403.3	405.0	342.9	343.5
July	1.448	1.402	1.033	1.004	1.330	1.361	404.6	405.1	343.5	343.0
August	1.450	1.384	1.035	0.996	1.353	1.329	404.7	402.4	342.7	340.2
September	1.431	1.395	1.026	0.993	1.342	1.334	404.5	403.1	341.6	339.9
October	1.406	1.386	1.011	0.972	1.316	1.326	404.6	403.3	341.1	339.5
November	1.394	1.392	0.989	0.965	1.309	1.320	404.7	404.6	340.7	340.0
December	1.380	1.385	0.964	0.967	1.296	1.309	404.4	405.1	339.8	339.6

	Non-Residential		Public Construction		Residential Construction	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	129.7	129.7	79.2	79.3	189.4	192.8
August	127.8	130.4	77.5	76.7	190.8	195.8
September	129.4	129.6	79.5	79.0	192.7	196.9
October	128.8	129.5	79.8	80.9	190.6	198.9
November	128.1	129.9*	80.0	82.2*	189.3	199.9*
December	127.5	129.2	80.1	81.6	188.0	200.7
January 1989	128.6	128.5	80.8	81.0	189.5	198.0
February	129.2	128.1	81.4	81.3	190.7	196.4
March	129.8	127.2	82.0	81.9	192.0	193.5
April	129.5	127.4	82.3	82.6	192.0	193.3
May	129.3	127.2	82.5	83.0	191.6	194.3
June	129.3	126.5	82.8	83.5	191.2	195.0
July	129.0	126.6	83.0	83.8	192.6	194.7
August	128.5	126.3	82.9	83.2	193.3	192.9
September	128.0	126.5	83.3	83.7	193.2	192.9
October	128.4	126.2	83.6	84.1	192.6	193.0
November	129.0	125.9	83.9	84.5	191.8	194.2
December	129.3	126.1	84.1	84.8	191.0	194.2

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BUSINESS ACTIVITY

	Manufacturers' Inventories		Durable Goods Orders		Non-Defense Capital Goods Orders		Non-Defense Capital Shipments	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	343.8	343.8	116.11	116.11	36.21	36.21	32.01	32.01
August	345.6	345.8	122.73	122.81	38.71	38.81	32.34	32.41
September	347.3	347.8	117.70	119.32	34.09	34.86	31.95	32.52
October	349.0	349.9*	119.23	122.06	34.65	33.81	32.37	32.57
November	350.3	351.5	118.51	120.61*	34.26	34.62*	32.65	32.69*
December	351.6	353.3	118.26	120.93	34.12	34.81	32.98	32.88
January 1989	353.3	354.8	116.94	117.45	33.04	33.95	32.86	32.85
February	355.4	356.5	117.72	117.27	33.26	33.65	33.07	33.17
March	357.5	358.2	118.84	118.14	33.49	33.84	33.29	33.26
April	359.0	360.0	119.93	119.48	33.76	34.12	33.41	33.45
May	360.2	361.8	119.52	119.93	33.95	34.27	33.48	33.61
June	361.5	363.6	120.21	118.85	33.28	33.96	33.53	33.68
July	364.0	365.1	119.46	118.42	33.72	33.75	33.60	33.65
August	366.3	366.7	119.93	119.07	34.16	33.92	33.69	33.74
September	368.5	368.2	119.65	120.16	34.20	34.16	33.78	33.81
October	370.3	370.0	119.27	120.93	34.17	34.29	33.92	33.90
November	372.5	371.5	119.04	120.45	34.13	34.20	34.06	33.96
December	374.8	373.2	117.86	122.16	33.65	34.35	34.05	34.17

	Business Inventories		Defense Shipments		Industrial Production		Capacity Utilization	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	735.9	735.9	8.66	8.66	138.1	138.0	83.8	83.7
August	741.7	743.9	9.02	9.04	138.3	138.4	83.8	83.8
September	744.7	749.4	8.74	8.83	138.3	138.7	83.6	83.8
October	749.6	752.4*	8.50	8.43	138.7	139.2	83.8	84.0
November	754.0	755.8	8.55	8.62*	139.1	139.8*	83.9	84.2*
December	758.4	759.7	8.60	8.75	139.5	140.3	84.1	84.4
January 1989	761.5	763.9	8.61	8.70	140.0	140.6	84.3	84.5
February	764.7	767.6	8.69	8.67	140.5	140.9	84.5	84.5
March	768.0	771.3	8.76	8.73	141.0	141.3	84.7	84.6
April	771.3	775.2	8.80	8.80	141.2	141.8	84.6	84.8
May	775.4	779.1	8.84	8.85	141.2	142.1	84.3	84.8
June	779.4	783.9	8.90	8.82	141.8	142.4	84.5	84.9
July	783.5	788.6	8.79	8.96	142.4	142.4	84.8	84.7
August	787.2	793.3	8.84	9.15	143.2	142.9	85.2	85.0
September	791.0	797.5	8.70	9.07	144.0	143.3	85.5	85.1
October	795.6	801.4	8.81	8.92	144.3	143.6	85.5	85.2
November	800.3	805.6	8.96	8.95	144.4	143.8	85.4	85.2
December	805.0	809.3	9.11	9.13	144.2	143.9	85.1	85.1

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PRICES

	CPI-U (seasonally adjusted)		PPI Finished Goods (seasonally adjusted)		PPI-Industrial Commodities (unadjusted)		Estimated GNP Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	118.5	118.5	108.3	108.3	106.7	106.7	121.9	122.0
August	119.0	119.0	108.9	108.9	107.1	107.1	122.2	122.3
September	119.4	119.4	109.3	109.3	106.9	106.9	122.7	122.8
October	119.9	119.9	109.2	109.5	107.2	107.1	123.0	123.3
November	120.4	120.4*	109.4	109.9*	107.5	107.6*	123.3	123.7
December	120.8	120.9	109.7	110.3	107.8	108.1	123.6	124.1
January 1989	121.1	121.4	110.3	110.8	108.0	108.4	124.1	124.6
February	121.4	121.8	110.6	111.2	108.1	108.9	124.6	125.0
March	121.8	122.3	110.9	111.5	108.2	109.0	125.2	125.4
April	122.3	122.7	111.2	111.8	108.7	109.2	125.6	125.9
May	122.8	123.1	111.5	112.1	109.4	109.6	125.9	126.3
June	123.4	123.6	111.8	112.4	110.1	110.9	126.2	126.8
July	124.0	124.1	112.2	112.8	110.5	111.3	126.7	127.3
August	124.6	124.7	112.6	113.3	110.8	111.7	127.1	127.7
September	125.2	125.2	113.0	113.7	110.5	110.9	127.5	128.3
October	125.7	125.8	113.4	114.1	111.2	112.1	128.0	128.8
November	126.2	126.4	113.9	114.5	111.9	112.5	128.4	129.3
December	126.8	127.0	114.5	115.0	112.6	112.9	128.8	129.9

	Consumption Deflator		Consumer Durables		Consumer Nondurables		Consumer Services		Implicit Construction Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	124.8	124.8	110.1	110.0	116.9	116.9	135.1	135.1	116.0	116.0
August	125.1	125.1	110.4	110.4	117.1	117.0	135.5	135.4	115.9	115.9
September	125.7	125.8	110.6	110.6	117.9	117.9	136.1	136.1	116.1	116.0
October	126.2	126.3	110.8	110.9	118.2	118.4	136.7	136.7	116.3	116.2
November	126.6	126.7*	110.7	111.0*	118.5	118.8*	137.2	137.3*	116.5	116.4*
December	127.0	127.2	110.9	111.2	118.9	119.2	137.8	137.9	116.7	116.6
January 1989	127.4	127.7	111.2	111.4	119.2	119.6	138.5	138.5	116.8	116.9
February	127.9	128.1	111.5	111.6	119.5	120.0	139.0	139.1	117.0	117.1
March	128.4	128.6	111.8	111.9	119.8	120.4	139.5	139.6	117.2	117.3
April	129.0	129.1	112.0	112.1	120.5	120.8	140.1	140.2	117.4	117.5
May	129.8	129.5	112.0	112.3	121.3	121.1	140.8	140.8	117.4	117.7
June	130.0	130.1	112.2	112.5	122.0	121.5	141.5	141.5	117.6	117.9
July	130.7	130.6	112.5	112.7	122.3	122.0	142.0	142.1	117.8	118.1
August	131.1	131.1	112.9	113.0	122.6	122.5	142.6	142.7	118.1	118.3
September	131.4	131.6	113.3	113.4	122.9	123.0	143.2	143.3	118.4	118.6
October	132.1	132.2	113.5	113.6	123.6	123.5	143.8	144.0	118.6	118.8
November	132.6	132.8	113.4	113.8	124.2	124.1	144.4	144.6	118.8	119.0
December	133.1	133.4	113.6	114.0	124.8	124.7	145.0	145.3	119.0	119.3

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MISCELLANEOUS

	Merchandise Trade Balance		Leading Indicators		Estimated GNP		Estimated GNP (1982 $)		IVA (annual rate)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	-9.98	-9.98	192.7	192.4	4888	4891	4010	4009	-27.2	-28.6
August	-10.53	-10.53	193.4	193.4	4900	4906	4010	4011	-23.7	-30.4
September	-8.97	-8.97	193.6	192.9	4915	4931	4006	4015	-18.5	-32.8
October	-9.28	-9.28*	194.2	193.0	4935	4962	4012	4024	-20.6	-27.4
November	-9.65	-9.93	194.5	192.6*	4954	4986	4018	4031	-21.9	-23.7
December	-10.02	-10.17	193.7	193.0	4974	5007	4024	4035	-23.2	-27.5
January 1989	-8.76	-9.65	194.0	193.3	5016	5067	4042	4067	-16.5	-30.5
February	-7.93	-9.40	194.4	193.2	5066	5098	4066	4078	-14.8	-30.9
March	-7.39	-9.26	194.0	193.5	5107	5128	4079	4089	-13.0	-27.6
April	-7.05	-9.43	193.5	193.7	5127	5159	4082	4098	-17.6	-23.2
May	-7.38	-8.89	193.1	193.8	5148	5182	4089	4103	-19.9	-21.9
June	-7.34	-8.26	193.5	193.5	5169	5214	4096	4112	-22.3	-18.3
July	-8.21	-8.84	193.8	193.2	5194	5235	4099	4115	-22.1	-19.8
August	-8.46	-8.59	193.2	193.0	5221	5255	4108	4127	-22.6	-20.5
September	-8.65	-8.63	192.7	193.2	5248	5303	4116	4133	-23.1	-21.7
October	-7.73	-8.14	192.0	192.6	5279	5327	4124	4136	-26.9	-23.8
November	-7.27	-7.64	191.6	192.0	5301	5352	4129	4139	-28.0	-24.6
December	-6.80	-7.36	192.1	191.5	5323	5378	4133	4140	-29.1	-25.5

	Currency Index		Adjusted Profits		30-Year Government Bonds		New York Composite	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	96.53	96.53	191.2	186.2	9.14	9.14	152.12	152.12
August	98.29	98.29	188.5	178.5	9.32	9.32	149.25	149.25
September	97.91	97.91	183.7	174.7	9.06	9.06	151.47	151.47
October	94.63	95.10	173.5	176.3	9.01	8.89	157.63	156.24
November	90.46	91.91	166.7	178.4	9.17	9.02	160.26	152.46
December	87.01	90.43*	160.5	180.5	9.30	9.03*	160.63	155.83*
January 1989	85.56	91.86	169.8	182.9	9.24	9.10	161.25	157.42
February	88.42	92.95	173.8	185.3	9.26	9.07	162.29	161.36
March	91.26	91.02	177.7	187.6	9.25	8.96	162.05	164.14
April	92.15	89.26	175.2	184.5	9.30	9.14	154.43	161.25
May	90.45	87.75	173.8	183.1	9.33	9.23	149.62	160.57
June	91.03	86.64	172.5	178.6	9.52	9.30	145.15	156.59
July	91.72	88.23	174.0	179.4	9.65	9.45	143.65	153.65
August	92.43	89.74	174.9	175.3	9.54	9.48	152.43	154.18
September	93.06	90.52	173.6	173.2	9.59	9.50	153.11	152.28
October	92.20	91.86	169.4	169.4	9.73	9.41	149.25	149.67
November	89.25	90.20	167.8	169.9	9.88	9.26	147.85	151.43
December	86.93	87.46	166.2	169.8	10.03	9.11	142.25	153.62

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FINANCIAL MARKETS

	Monetary Base		M1		M2		Federal Funds		T-Bills (6 Mos.)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	280.3	280.2	782.4	782.3	3025.9	3025.8	7.75	7.75	6.99	6.99
August	281.1	281.1	782.5	782.5	3031.8	3031.6	8.01	8.01	7.36	7.36
September	282.1	282.3	782.5	782.3	3035.1	3034.1	8.19	8.19	7.43	7.43
October	284.0	283.4	785.3	783.5	3043.5	3037.2	8.25	8.30	7.36	7.50
November	285.3	285.1*	792.6	784.2*	3079.0	3053.5*	8.23	8.35	7.37	7.76
December	286.6	286.7	799.3	787.6	3106.5	3071.8	8.22	8.62*	7.37	7.95*
January 1989	288.4	288.4	803.1	791.1	3120.4	3090.2	8.20	8.55	7.35	7.90
February	290.2	290.0	805.3	794.6	3134.5	3108.7	8.18	8.63	7.36	7.94
March	291.9	291.6	807.6	799.0	3148.6	3130.5	8.22	8.60	7.37	7.92
April	293.7	293.1	811.9	803.1	3167.7	3149.3	8.24	8.54	7.40	7.85
May	295.0	294.6	817.7	807.8	3188.6	3171.3	8.25	8.75	7.46	8.03
June	296.3	296.0	823.2	811.9	3208.9	3193.5	8.35	8.88	7.55	8.16
July	298.0	297.5	826.9	816.6	3229.3	3215.9	8.33	9.03	7.52	8.24
August	299.5	299.4	831.4	820.9	3249.1	3238.4	8.30	9.02	7.40	8.20
September	300.9	301.3	834.9	825.6	3268.8	3261.1	8.36	9.05	7.42	8.25
October	302.5	303.0	838.6	829.3	3281.4	3280.7	8.55	9.26	7.69	8.34
November	304.3	304.8	842.9	833.6	3299.1	3300.4	8.92	9.24	7.89	8.27
December	306.0	306.2	847.3	835.9	3317.6	3316.9	9.03	9.18	8.01	8.10

	Aaa (Seasoned)		Municipals (Bond Buyer)		(3 Month) Commercial Paper		90 Day CD's		Prime Rate	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	9.96	9.96	7.76	7.76	7.82	7.82	7.94	7.94	9.29	9.29
August	10.11	10.11	7.79	7.79	8.26	8.26	8.35	8.35	9.84	9.84
September	9.82	9.82	7.66	7.66	8.17	8.17	8.23	8.23	10.00	10.00
October	9.68	9.51	7.49	7.47	8.23	8.24	8.30	8.36	10.00	10.00
November	10.01	9.45	7.80	7.46	8.24	8.66	8.32	8.78	10.00	10.05
December	10.17	9.56*	7.85	7.55*	8.29	8.94*	8.38	9.03*	10.00	10.50*
January 1989	10.05	9.63	7.82	7.62	8.25	8.65	8.33	8.79	10.00	10.50
February	10.08	9.60	7.83	7.65	8.26	8.69	8.35	8.84	10.00	10.50
March	10.10	9.54	7.87	7.54	8.24	8.66	8.33	8.76	10.00	10.50
April	10.15	9.76	7.92	7.71	8.27	8.47	8.40	8.60	10.00	10.50
May	10.20	9.87	7.95	7.82	8.30	8.71	8.41	8.83	10.00	10.66
June	10.24	10.03	7.98	7.99	8.37	8.89	8.46	9.01	10.00	11.00
July	10.33	10.26	8.04	8.05	8.39	9.11	8.50	9.22	10.00	11.15
August	10.38	10.35	8.08	8.16	8.42	9.10	8.56	9.25	10.00	11.50
September	10.45	10.30	8.15	8.11	8.45	9.12	8.60	9.23	10.00	11.50
October	10.62	10.24	8.31	8.05	8.66	9.20	8.73	9.34	10.46	11.50
November	10.73	10.15	8.40	8.03	9.03	9.22	9.15	9.36	10.75	11.50
December	10.82	10.02	8.46	7.98	9.15	9.15	9.26	9.28	11.00	11.50

Fore. = November Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

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MONTHLY PROJECTIONS
December 1988

Dr. Donald Ratajczak, Director
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WHAT DOES THE HUMPED YIELD-CURVE MEAN?

In the past few months, interest rates on short-term securities have continued to rise while interest rates with long-term maturities have begun falling. Although interest rates at the very short end of the yield structure remain below long-term yields, thus preventing the curve from being totally inverted, a significant hump in yields has developed beginning at one year of maturity and rising until seven years of maturity. Yields than fall through thirty years.

One explanation for this hump is that the Federal Reserve has been restraining reserve growth in commercial banks in order to reduce inflationary pressures. In the scramble for reserves, banks have been selling their short-term instruments, leading to increased supply and higher rates at that end of the yield spectrum. At the same time, investors have become encouraged that the Federal Reserve restraint will, in fact, lead to inflationary restraint. Thus, they are increasingly attracted to yields at the long end of the spectrum because the inflationary premiums necessary to compensate for purchasing power risk are coming down.

Unfortunately, the major fallacy in the above reasoning is that such Federal Reserve restraint would lead to a total inversion of the yield curve. If the point of restraint is bank reserves, sharply higher federal funds rates would lead to significant increases in treasury bill yields that eventually would exceed yields on long-term instruments. This does not explain why the yield curve is humped.

An alternative explanation can be based upon expectations of investors. As the year began, the consensus forecast was that inflationary pressures would continue to accelerate during the first half of 1989. This would be created by rising pressures on wage compensation. Such interest rate pressures may lead to further Federal Reserve restraint and higher short-term interest rates. Thus, investors with short-term investment desires would seek an unusually short maturity for their portfolios. At the same time, the Federal Reserve restraint was expected to eventually slow economic activity and inflationary pressures. Thus, the long end of the maturity structure also would decline.

While such expectations probably are responsible for the current hump in the yield curve, there is no reason to expect that those expectations will be realized. It is unusual for inflationary pressures to reach a peak and then decline with only a moderation in the growth of the economy. This is especially so if the inflationary pressures are coming from the wage cost side of the system. In fact, short-term indicators of inflationary pressures have been modestly favorable. The fastest declining components of the leading indicators have been vendors' deliveries, sensitive prices, and the inflation-adjusted money stock. All these variables are leading indicators of inflationary trends. Of course, the sensitive indicators followed by the Journal of Commerce have accelerated in recent weeks. In addition, sensitive prices in the PPI at the earliest stages of processing also have intensified.

My own interpretation of these trends is that inflationary pressures early in 1989 will not be as high as the consensus forecast assumes. As a result, those investing in the long end of the yield spectrum will initially feel relieved by reduced inflationary prospects. However, price pressures by stage of processing suggest that underlying inflationary pressures have not receded. Indeed, inflation may intensify later in the year. If so, the Federal Reserve may tighten credit market conditions at that time. Thus, investments in long-term instruments probably only make sense if investors are willing to turn over their positions after garnering a near-term profit. If that proves to be correct, long-term interest rates will be rising faster than other components of the yield spectrum, especially the intermediate term securities, by mid-year.

Clearly, the humped yield curve suggests that the budgetary assumptions used in President Reagan's final budget submission to the Congress are inappropriate. In that document, treasury bill rates were expected to average 6.3%. They are now two percentage points higher than that level, which should add nearly $12 billion to the deficit. Also, inflationary pressures were expected to recede by nearly a percentage point. If our analysis is correct, inflation will average a half percentage point higher in 1989 than in 1988 and will be growing more than a percentage point more rapidly toward the end of the year. Because of cost of living adjustments contained in the budget, this would add another $10- $12 billion to the deficit.

Budget revenue estimates also show no awareness of the shifting financial structure that is sharply diminishing the taxable earnings from capital. More than $4 billion of tax incentives were used to encourage the infusion of new capital investment in the savings and loan industry. Also, corporate financial restructurings are converting equity into debt. The result will be a reduction in corporate tax payments. While there will be some offsetting increase in household tax payments through increased interest earnings, the marginal tax rate for households is lower than the marginal tax rate for the corporate sector. As a result, this corporate financial restructuring will probably reduce revenues by several billions. Clearly, corporate tax receipts will not increase by the $13 billion currently projected for the next fiscal year.

Probably a little should be said about the expenditures reductions proposed by President Reagan. Most of the 82 agencies that are slated for elimination in the Reagan budget already have been considered by Congress. There is little likelihood that they will reverse their opinions and now decide to agree with the President. An additional $5 billion reduction in farm programs will require new farm legislation. There appears to be little desire to open the farm bill at this time. Providing less than the cost of living adjustment for government retirees almost certainly will be viewed as unfair and a precursor of similar action for social security recipients. As a result, such adjustments are not anticipated. Even the pay scale of government employees is open to some question. The budget proposes only a 2% increase for civilian personnel and a 3.5% increase for the military. Given wage gains projected to exceed 5% in the private economy, such proposals almost certainly will lead to turnover and reduced quality of the government work force.

When the expenditures proposals are adjusted for probable outcomes, including the likelihood that Congress will provide no inflation growth for defense, (the president proposed a 2% real growth in defense spending), expenditures probably will exceed budget proposals by $40 billion. With revenues falling short by nearly $10 billion as a result of corporate restructurings, the deficit should be $40 billion higher than the $90 billion proposed by President Reagan. This will not be in conformity with Gramm-Rudman guidelines, although it will be an improvement from the previous year.

Quarterly Profile of GNP

	1988-3	1988-4	1989-1	1989-2	1989-3	1989-4	1988 Annual	1989 Annual
Real:	2.5	1.9	5.2	2.0	2.3	1.9	3.8	2.9
Price:	4.7	4.3	4.3	4.2	4.8	4.8	3.3	4.5
Nominal:	7.3	6.3	9.6	6.4	7.3	6.8	7.3	7.5

Monthly Statistical Highlights for December 1988

Personal income +0.6%; savings rate 4.0%; personal consumption +0.9%; housing starts -4.4%; housing permits -3.1%; construction expenditures -0.7%; business inventories +0.5%; orders for durable goods -0.7%; orders for nondefense capital goods -4.0%; industrial production +0.1%; CPI +0.4%; consumption deflator +0.3%; leading indicators -0.3%; real GNP(AR) +2.4%.

Monthly Statistical Highlights for January 1989

Payroll employment +227,000; index of hours worked +0.2%; household employment +186,000; civilian unemployment rate 5.3%; personal income +0.4%; savings rate 4.2%; personal consumption +0.5%; retail sales -0.3%; auto sales 10.5 million units; housing starts UNC; housing permits -2.1%; construction expenditures -0.3%; business inventories +0.5%; orders for durable goods -0.8%; orders for nondefense capital goods -1.6%; industrial production +0.2%; CPI +0.3%; PPI +0.3%; consumption deflator +0.4%; leading indicators +0.2%; currency index +0.5%; equity index +5.1%; real GNP(AR) 11.6%; M1(AR) 11.4%; M2(AR) +5.1%.

Commentary

Employment - Once again, a surge in part-time employment led to a nearly 280,000 increase in payroll employment while the workweek actually declined. In manufacturing, the workweek fell by 0.2 hours. Therefore, the index of hours worked barely changed. Nevertheless, the index of hours worked increased 3.7% at annual rates during the fourth quarter. Assuming moderate gains in productivity and a drought effect of nearly 1.5 percentage points, this would lead to slightly more than 2% GNP growth.

Although civilian employment grew very slowly, even slower growth in the labor force led to a slight decline in the unemployment rate. It is unlikely that strong employment growth leading to significant declines in unemployment will develop in January.

Equally significant, the hourly earnings index showed only a modest increase. For the quarter, the hourly earnings index rose 4.1%. This is an acceleration from earlier in the year, but the rate of wage increase remains modest. Although these employment figures are consistent with an economy slowing significantly during the quarter, our GNP components suggest that the greatest slowing is occurring in inventory accumulations. This reduction may be the result of expected weak Christmas sales, expectations that were not justified. As a result, production should spurt early in 1989.

Personal Income and Outlays - An unusually sharp drop in farm subsidies, leading to only $15 billion in farm income, accounted for a rare decline in personal income during November. The wage component also was sluggish. As a result of the sharp decline in farm earnings, personal savings dropped sharply. Of course, some gains in farm income from these unusually low levels should be expected in the months ahead. The wage component, on the other hand should continue to grow at a sluggish rate as long as part-timers are the major thrust behind what employment growth is materializing.

The advanced retail sales report for December did not capture the sharp spurt in auto sales that developed in the last ten days of the month. When more complete information is available next month, a significant upward revision is anticipated in retail sales estimates. A decline in purchases of food products possibly reflects some weakening of food prices in December. By the time the personal income report is released, more information should be available on automobile sales, leading to a significant spurt in sales of durable goods. A return to more appropriate winter weather also should lead to a rebound in service expenditures growth. Thus, consumer outlays are expected to exceed previously forecasted values during the fourth quarter. In effect, while economic activity was exhibiting anticipated strength, consumer spending was stronger while inventory accumulations were weaker than anticipated. This usually is a prescription for stronger production activity ahead.

Construction - Favorable building weather was apparent in the construction statistics for November. Housing permits were stronger than anticipated as starts of apartment units took advantage of the favorable weather. In addition, a surge in sales on the West Coast led to a spurt in single-family activity. However, sharply weakening prices and sales in New England should impact single-family starts in December and January. More seasonal weather also should significantly slow housing activity during the winter months.

Even with favorable weather conditions, nonresidential construction fell in November. This suggests that further reductions will be taking place in that sector in the months ahead. Some correction from weather-induced public construction activity is expected in December, but significant activity in single-family housing should persist into the winter months. This strength in housing is only temporary, however. Although activity currently is well above forecasted levels, activity is expected to slow and fall below forecasted levels during the second half of 1989. This will occur as interest rates rise at that time.

Inflation in construction materials remains modest. The construction cost index showed no increase in November after growing 0.2% in the previous month. Only modest increases in construction costs are anticipated during next year.

Business Activity - Commercial aircraft continued to buoy orders for capital goods in November. Those orders should sharply diminish in the next few months. As a result, a downtrend in orders for nondefense capital goods should materialize. However, machinery orders appear to be strengthening. Also, commercial aircraft orders should rebound later in the year. This suggests that shipments for nondefense capital goods will remain strong all year. Although shipments slowed slightly in November, this must be the result of temporary production restraints rather than the beginning of any serious downtrend.

Defense shipments, on the other hand, are continuing to show little growth following a summer spurt. Orders have improved slightly, which should lead to some acceleration in shipments. Nevertheless, shipments probably will only slightly exceed the rate of inflation over the next twelve months. Even slower shipments are expected beyond that.

Business inventories grew surprisingly slowly in October as a result of a decline in retail inventories. Retailers apparently became so cautious that they were willing to lose sales rather than overstock. This cautiousness probably led to only modest inventory accumulations during the fourth quarter. However, as sales exceeded anticipations, a more vigorous inventory buildup is expected early in 1989.

The employment situation indicated that activity slowed significantly in December. Production of consumer goods and defense goods both may have declined modestly in the month. However, a rebound in utilities, industrial materials, and business equipment probably allowed some growth in overall industrial production. Strong auto sales and the liquidation of retail inventories probably will lead to a rebound in industrial activity in the next few months.

Prices - The CPI grew even slower than had been anticipated in November as a result of larger-than-expected discounting of clothing prices. There continues to be a shift in seasonal prices in the clothing sector, which should lead to further modest discounting in December and January. Next year's seasonals probably will more fully capture the sharp surge in prices when new fashions are released followed by price discounting a few months later. Excluding the clothing component, the CPI has been growing in the 4% to 4.5% range that has prevailed since 1987 began.

The PPI is showing a bit more price intensity. A sharp increase in tobacco prices in December almost certainly will cause a modest spurt in the CPI in December and January. The removal of automobile incentives also should be reflected at the CPI level. However, sharp increases in energy components may have very little effect at the finished goods level. Thus, industrial commodities prices are growing faster than finished goods prices at the current time. Apparently, ample supplies of gasoline assure no change in that component until the driving season begins in the spring. If OPEC prices are declining at that time, as expected, energy prices may not be a factor in inflationary prospects for 1989.

Our current projections suggest that prices will continue along their current growth path through the first half of 1989. An acceleration then is anticipated in the second half largely as a result of higher wage cost pressures. In addition, the dollar, which has held its value in the last thirteen months, is expected to begin eroding in value in the second half of the year.

Miscellaneous - The trade deficit apparently worsened at the end of 1988. Both slowing in the growth of exports and acceleration in imports appear to be responsible. In addition, oil prices again are rising, exerting upward pressures upon that import component. However, the greatest reason for the higher trade deficit estimates in our forecast is the continued strength of the dollar. As a result of the dollar's strength, the competitiveness of American manufacturing has not improved during the past year. As foreign investors become aware that the merchandise trade balance no longer is declining significantly, the dollar is again expected to fall. Indeed, we are currently projecting that the dollar will fall more during 1989 than originally anticipated. Part of this decline will occur when it is also recognized that interest rates in the United States are not rising significantly during the first half of this year.

Higher oil prices will be reflected in a surge in the inventory valuation adjustment during the early months of 1989. This will have an adverse effect upon adjusted profits. However, stronger growth in nonfarm activity than anticipated in the quarterly forecast along with continued wage restraint should lead to higher operating profits less tax liabilities than originally projected.

As a result of improved profitability and reduced interest rate pressures, equity values should rise significantly early in the year. While equity values appear to be above what our valuation estimates suggest, no correction in this excess is likely while adjusted profits are rising and long-term interest rates are declining. Another 10%-15% increase in equity values is possible in the early months of 1989. Later in the year, however, rising interest rates and wage pressures along with slower economic growth should cause a decline in adjusted profits. In that context, equity values should decline.

Financial Markets

Clearly, President Reagan's budget requests will not be enacted. In addition, the interest rate estimates are understating interest expenditures by more than $12 billion while tax incentives associated with the savings and loans bailout and LBO financing restructuring, which substitutes debt for equity, almost certainly assures a substantial shortfall in the corporate tax receipts estimated in the Reagan budget - probably as much as $10 billion. Therefore, government deficits in excess of $140 billion appear likely next year. However, the budget deficit currently is in excess of $155 billion. Therefore, some modest deficit reduction could develop in the latter months of 1989.

However, these deficit estimates do not include borrowings by bank agencies in order to ease cash flow problems in managing thrift industry difficulties. The budget assumes $10 billion of additional borrowings, but borrowings of twice that magnitude probably will surface. As a result, total government borrowings may rise slightly next fiscal year.

Because of strong consumer spending and continuing growth in housing purchases, especially on the West Coast, there appears to be little improvement in the net savings behavior of the household sector. Installment credit is continuing to grow about 8%, slightly faster than the growth in disposable income. Later in 1989, falling housing sales probably will cause a reduction in the growth of mortgage debt, leading to a rise in effective household savings.

Together, the household and government sectors suggest little direction for interest rate pressures early in the year but some moderation in those pressures in the latter stages of the year.

However, corporate borrowings for capital spending and inventory purposes are expected to intensify as the year progresses. Capital spending programs appear to be stronger earlier in the year than in the latter part of the year. This will coincide with acceleration in corporate cash flow, suggesting that the corporate sector may generate little upward pressure on the credit markets in winter and early spring. If capital spending slows significantly later in the year, it is conceivable that the corporate sector may not exert upward pressures on credit markets throughout the year. However, a more likely condition is that capital spending will remain moderately strong throughout the year while rising inflationary pressures in the second half of the year will encourage inventory accumulation. At the same time, rising interest rates and wage pressures will diminish the growth in corporate cash flow. The net effect would be a significant squeeze on corporate liquidity leading to gains in outside borrowings. Thus, the corporate sector's borrowing needs in the second half of the year probably will exert significant upward pressures upon interest rates.

Of course, foreign investors could offset these domestic credit market pressures in 1989. With a strong dollar and high real rates of interest, foreign investors probably will be attracted to American assets. Thus, foreign investors could hold interest rates down or even force them slightly lower. However, as trade balances start to deteriorate, foreign investors are expected to become increasingly disenchanted with their American investments. If they withdraw from American assets in the second half of the year, interest rate pressures will move significantly higher in order to retain those assets.

As a result, the consensus forecast of rising interest rates followed by falling rates later in the year is unlikely. Instead, interest rates probably will remain unchanged or even drift slightly downward early in the year. When corporate borrowings intensify later in the year for inventory purposes, however, domestic pressures will increase. In addition, some dollar weakness could lead to foreign investors withdrawing from the American markets, at least until real rates are pushed upward. Thus, rising interest rates in the second half of the year are likley.

Equity Markets - As mentioned above, economic conditions are favorable for an increase in equity values early in 1989. Interest rates should remain stable or even drift slightly lower in terms of long-term maturities while corporate profits are expected to continue rising. Later in the year, however, economic conditions are expected to reverse. Thus, a Dow Jones rise to more than 2300 in the spring could be followed by a dip to less than 2000 by late fall.

At the present time, the industries still showing capability of generating significant profit gains are chemicals, nonelectrical machinery, commercial aircraft, and some nonferrous metals. Strong cash flow suggests that utilities also will perform well early in the year while some regional banks should do satisfactorily. In addition, many consumer groups should do well because of stronger consumer activity than previously anticipated. On the other hand, the plastics, rubber, paper and textile industries no longer are showing the capacity pressures that helped to improve their profit margins earlier in the year. Therefore, those groups will struggle. Also, the technology group is suffering some sales erosion as potential customers are waiting for new technologies to become available. The technology groups are more likely to perform well in the second half of the year, but that will be bucking a downward trend in overall equity values.

Unfortunately, the current desire to invest in cyclical stocks could be treacherous, especially if the economy slows in the second half of the year. Furthermore, consumer-based issues, which will be responding to better-than-anticipated sales early in the year, could come under increasing downward valuation pressures as the 1989 Christmas season approaches. Thus, substantial adjustments probably will be necessary after mid-year to insure that consumer and cyclical stocks are not heavily weighted in portfolios. Nevertheless, the first half of 1989 should prove to be advantageous to most equity investors.

EMPLOYMENT

	Payroll Employment		Index of Hours Worked		Household Civilian Employment		Civilian Unemployment Rate		Hourly Earnings Index	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	106271	106271	126.4	126.4	115059	115059	5.4	5.4	179.3	179.3
August	106440	106425	125.5	125.5	115180	115203	5.6	5.6	179.6	179.5
September	106695	106737	126.0	126.0	115328	115370	5.4	5.4	180.4	180.3
October	106895	106973	126.3	127.1	115587	115573	5.3	5.3	181.0	181.5
November	107144	107377	126.7	127.0	115895	115947	5.2	5.4	181.5	181.4
December	107393	107656	127.1	127.1	116207	116009	5.2	5.3	182.1	181.7
January 1989	107608	107883*	127.4	127.3*	116443	116195*	5.1	5.3*	182.8	182.2*
February	107840	108136	127.7	127.6	116666	116463	5.0	5.2	183.5	182.6
March	108072	108456	127.9	128.0	116889	116756	5.0	5.1	184.3	183.1
April	108246	108710	128.1	128.3	117003	117003	5.0	5.0	184.9	183.6
May	108419	108983	128.4	128.6	117219	117264	4.9	5.0	185.4	184.2
June	108592	109322	128.5	129.0	117435	117554	5.0	4.9	186.0	184.7
July	108756	109529	128.7	129.2	117568	117756	4.9	4.9	186.7	185.3
August	108913	109792	128.9	129.5	117723	118006	4.9	4.8	187.4	185.9
September	109070	109962	129.1	129.7	117884	118185	4.8	4.8	188.2	186.5
October	109216	110169	129.2	129.9	118005	118382	4.8	4.8	188.9	187.1
November	109352	110300	129.3	130.0	118229	118543	4.9	4.9	189.5	187.8
December	109488	110395	129.2	130.1	118445	118644	4.9	4.9	190.2	188.5

PERSONAL INCOME

	Personal Income		Wage & Salary		Personal Savings		Disposable Income		Personal Outlays	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	4.071	4.075	2.452	2.452	141.0	149.1	3.487	3.491	3.346	3.342
August	4.083	4.092	2.457	2.459	132.4	133.3	3.497	3.506	3.365	3.373
September	4.103	4.115	2.471	2.475	147.5	154.5	3.513	3.526	3.366	3.371
October	4.133	4.184	2.484	2.512	148.0	182.9	3.535	3.587	3.387	3.404
November	4.158	4.175	2.500	2.520	152.0	153.3	3.557	3.577	3.405	3.423
December	4.182	4.200*	2.516	2.528*	157.2	145.1*	3.579	3.599*	3.422	3.454*
January 1989	4.204	4.215	2.535	2.540	173.4	151.7	3.612	3.623	3.439	3.471
February	4.238	4.239	2.550	2.554	168.1	161.2	3.630	3.648	3.462	3.487
March	4.270	4.264	2.565	2.570	163.0	167.1	3.645	3.672	3.482	3.505
April	4.286	4.289	2.580	2.585	159.2	169.0	3.661	3.693	3.502	3.524
May	4.300	4.314	2.592	2.601	157.4	170.8	3.678	3.715	3.521	3.544
June	4.314	4.341	2.604	2.618	155.5	176.6	3.695	3.739	3.540	3.562
July	4.340	4.364	2.619	2.632	152.3	180.6	3.711	3.758	3.559	3.577
August	4.365	4.391	2.634	2.649	149.2	179.8	3.725	3.782	3.576	3.602
September	4.390	4.415	2.649	2.663	146.3	181.1	3.739	3.802	3.593	3.621
October	4.408	4.439	2.660	2.678	146.9	185.0	3.756	3.822	3.609	3.637
November	4.429	4.462	2.673	2.691	148.5	194.5	3.778	3.841	3.630	3.647
December	4.450	4.487	2.687	2.705	145.1	195.1	3.797	3.862	3.652	3.667

Fore. = November Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

CONSUMPTION

	Personal Consumption		Durables		Nondurables		Services		Consumption Real	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	3245.3	3238.9	454.4	448.5	1053.0	1053.0	1737.9	1737.4	2600.1	2594.8
August	3263.4	3271.1	454.8	455.5	1059.6	1064.4	1749.0	1751.2	2608.1	2615.1
September	3264.1	3270.2	451.7	450.8	1060.0	1065.0	1752.4	1754.4	2595.8	2599.1
October	3283.7	3302.9	454.3	450.5	1065.6	1072.5	1763.8	1779.9	2601.1	2613.6
November	3301.3	3321.6	457.2	457.4	1067.9	1079.4	1776.2	1784.8	2607.4	2619.7*
December	3319.0	3352.0*	455.3	474.1*	1070.3	1084.3	1793.4	1793.6*	2613.6	2634.9
January 1989	3338.3	3369.0	460.1	474.6	1073.5	1089.5	1804.7	1804.9	2620.5	2638.5
February	3356.5	3384.0	463.7	473.2	1077.4	1094.5	1815.4	1816.3	2623.9	2641.1
March	3374.2	3401.7	467.0	476.2	1081.9	1098.6	1825.3	1826.9	2627.3	2645.0
April	3401.3	3420.3	469.9	479.5	1088.5	1102.0	1842.9	1838.8	2635.9	2650.6
May	3423.6	3440.0	473.4	481.0	1097.7	1108.6	1852.5	1850.4	2537.2	2655.3
June	3421.0	3457.1	459.8	481.1	1106.8	1115.7	1854.4	1860.3	2630.8	2658.2
July	3447.5	3471.9	465.6	478.4	1112.4	1123.6	1869.5	1869.9	2637.5	2657.6
August	3468.8	3495.6	470.4	483.1	1113.1	1130.0	1885.3	1882.5	2646.2	2664.7
September	3489.9	3514.2	475.1	483.2	1114.0	1135.4	1900.8	1895.6	2655.0	2669.0
October	3506.2	3529.7	473.4	481.2	1120.6	1141.2	1912.2	1907.3	2653.2	2669.7
November	3520.7	3538.6	470.2	482.5	1129.1	1146.7	1921.4	1909.4	2654.4	2665.7
December	3534.9	3558.4	470.1	483.5	1137.7	1152.3	1927.1	1922.6	2655.7	2669.2

RETAIL SALES

	Retail Sales		Non-Auto Durables		Auto (Million Units)		Nondurable Sales		Auto Sales	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	134.34	134.34	20.86	20.86	10.8	10.8	83.59	83.59	29.89	29.89
August	134.18	134.76	20.79	20.87	10.6	10.6	84.16	84.50	29.23	29.39
September	133.66	134.34	20.87	20.82	10.7	10.5	84.14	84.54	28.66	28.97
October	134.40	136.53	20.79	20.75	10.2	9.8	84.59	85.47	29.03	30.31
November	135.10	138.05	20.67	21.05	10.5	10.2	84.77	86.08	29.66	30.92
December	135.64	140.19*	20.85	21.02*	10.7	11.1*	84.96	86.32*	29.83	32.85*
January 1989	136.06	139.78	20.91	20.98	10.7	10.5	85.21	86.73	29.94	32.07
February	136.57	140.65	20.92	21.14	10.8	10.6	85.52	87.13	30.13	32.38
March	137.09	141.32	21.16	21.23	10.7	10.7	85.88	87.46	30.05	32.63
April	137.83	141.97	21.21	21.30	10.7	10.8	86.40	87.73	30.22	32.94
May	138.84	142.65	21.38	21.38	10.7	10.8	87.13	88.25	30.33	33.02
June	138.66	143.24	20.86	21.53	10.5	10.7	87.85	88.82	29.95	32.89
July	139.35	143.56	20.97	21.46	10.5	10.6	88.30	89.45	30.08	32.65
August	139.53	144.60	21.23	21.48	10.3	10.8	88.35	89.96	29.95	33.16
September	139.69	145.04	21.46	21.50	10.2	10.5	88.43	90.39	29.80	33.15
October	140.86	145.28	21.35	21.43	10.2	10.3	88.95	90.85	30.56	33.00
November	141.18	145.87	21.10	21.45	10.1	10.3	89.62	91.29	30.46	33.13
December	142.15	146.42	20.99	21.38	10.3	10.4	90.31	91.73	30.85	33.31

Fore. = November Forecast
C.E. = Current Expectations
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CONSTRUCTION

	Housing Starts		Single Family Starts		Housing Permits		Construction Expenditures (Current)		Construction Expenditures (Real)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	1.477	1.477	1.075	1.068	1.420	1.420	398.3	401.8	343.4	346.4
August	1.431	1.461	1.068	1.078	1.464	1.464	396.1	403.2	341.7	347.6
September	1.453	1.467	1.050	1.045	1.399	1.394	401.6	406.9	345.9	349.7
October	1.465	1.542	1.067	1.112	1.413	1.516	399.2	407.8	343.3	349.8
November	1.430	1.563	1.052	1.151	1.378	1.517	397.4	411.1	341.1	352.6
December	1.433	1.495*	1.043	1.105*	1.385	1.470*	395.6	408.2*	339.0	349.2*
January 1989	1.442	1.495	1.056	1.093	1.372	1.439	398.9	406.8	341.5	347.4
February	1.435	1.462	1.071	1.065	1.359	1.386	401.3	404.6	343.0	344.9
March	1.463	1.448	1.062	1.072	1.384	1.374	403.8	402.7	344.5	343.0
April	1.439	1.466	1.045	1.070	1.359	1.379	403.8	402.3	344.0	342.1
May	1.442	1.456	1.036	1.062	1.365	1.385	403.4	403.3	343.6	342.7
June	1.426	1.452	1.030	1.053	1.329	1.362	403.3	403.6	342.9	342.3
July	1.448	1.429	1.033	1.026	1.330	1.351	404.6	402.0	343.5	340.4
August	1.450	1.382	1.035	0.994	1.353	1.308	404.7	400.1	342.7	337.9
September	1.431	1.362	1.026	0.973	1.342	1.292	404.5	397.2	341.6	334.9
October	1.406	1.359	1.011	0.965	1.316	1.278	404.6	395.8	341.1	333.2
November	1.394	1.361	0.989	0.962	1.309	1.279	404.7	396.3	340.7	332.7
December	1.380	1.350	0.964	0.966	1.296	1.284	404.4	396.8	339.8	332.6

	Non-Residential		Public Construction		Residential Construction	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	129.7	129.7	79.2	79.3	189.4	192.8
August	127.8	130.4	77.5	76.9	190.8	196.0
September	129.4	130.3	79.5	79.7	192.7	196.9
October	128.8	130.9	79.8	77.9	190.6	199.0
November	128.1	129.7	80.0	80.9	189.3	200.4
December	127.5	128.4*	80.1	79.5*	188.0	200.3*
January 1989	128.6	128.1	80.8	79.8	189.5	198.9
February	129.2	128.3	81.4	80.5	190.7	195.8
March	129.8	128.0	82.0	80.3	192.0	194.4
April	129.5	127.4	82.3	80.9	192.0	194.0
May	129.3	127.6	82.5	81.3	191.6	194.4
June	129.3	127.1	82.8	81.6	191.2	194.9
July	129.0	126.6	83.0	82.3	192.6	193.1
August	128.5	126.3	82.9	82.5	193.3	191.3
September	128.0	125.6	83.3	83.0	193.2	188.6
October	128.4	125.7	83.6	83.4	192.6	186.7
November	129.0	125.4	83.9	83.7	191.8	187.2
December	129.3	125.5	84.1	83.9	191.0	187.4

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BUSINESS ACTIVITY

	Manufacturers' Inventories		Durable Goods Orders		Non-Defense Capital Goods Orders		Non-Defense Capital Shipments	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	343.8	343.8	116.11	116.11	36.21	36.21	32.01	32.01
August	345.6	345.8	122.73	122.81	38.71	38.81	32.34	32.41
September	347.3	347.8	117.70	119.32	34.09	34.86	31.95	32.52
October	349.0	349.4	119.23	122.79	34.65	34.62	32.37	32.69
November	350.3	350.9	118.51	122.77	34.26	35.67	32.65	32.43
December	351.6	353.4*	118.26	121.85*	34.12	34.23*	32.98	32.47*
January 1989	353.3	355.2	116.94	120.93	33.04	33.69	32.86	32.62
February	355.4	356.9	117.72	121.27	33.26	33.78	33.07	32.85
March	357.5	358.4	118.84	123.65	33.49	34.23	33.29	33.01
April	359.0	360.1	119.93	123.86	33.76	34.42	33.41	33.17
May	360.2	361.6	119.52	124.91	33.95	34.65	33.48	33.26
June	361.5	363.3	120.21	125.14	33.28	34.72	33.53	33.45
July	364.0	365.2	119.46	124.21	33.72	34.53	33.60	33.71
August	366.3	367.0	119.93	126.03	34.16	34.96	33.69	33.80
September	368.5	368.6	119.65	126.42	34.20	35.12	33.78	33.97
October	370.3	370.5	119.27	124.85	34.17	34.85	33.92	34.10
November	372.5	372.4	119.04	124.56	34.13	34.99	34.06	34.34
December	374.8	373.9	117.86	124.70	33.65	35.16	34.05	34.55

	Business Inventories		Defense Shipments		Industrial Production		Capacity Utilization	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	735.9	735.9	8.66	8.66	138.1	138.0	83.8	83.7
August	741.7	743.9	9.02	9.04	138.3	138.5	83.8	83.8
September	744.7	750.3	8.74	8.83	138.3	138.6	83.6	83.7
October	749.6	751.4	8.50	8.43	138.7	139.3	83.8	84.0
November	754.0	754.4*	8.55	8.55	139.1	139.9	83.9	84.2
December	758.4	757.9	8.60	8.63*	139.5	140.0*	84.1	84.1
January 1989	761.5	761.5	8.61	8.65	140.0	140.3	84.3	84.2
February	764.7	765.3	8.69	8.72	140.5	140.7	84.5	84.4
March	768.0	769.1	8.76	8.70	141.0	141.2	84.7	84.6
April	771.3	773.0	8.80	8.78	141.2	141.6	84.6	84.8
May	775.4	776.9	8.84	8.84	141.2	142.1	84.3	85.0
June	779.4	780.5	8.90	8.90	141.8	142.7	84.5	85.2
July	783.5	783.8	8.79	8.85	142.4	143.1	84.8	85.3
August	787.2	787.5	8.84	8.92	143.2	143.4	85.2	85.4
September	791.0	790.9	8.70	8.90	144.0	143.7	85.5	85.5
October	795.6	795.3	8.81	9.01	144.3	143.9	85.5	85.5
November	800.3	799.9	8.96	8.94	144.4	144.1	85.4	85.5
December	805.0	805.1	9.11	9.10	144.2	144.2	85.1	85.4

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PRICES

	CPI-U (seasonally adjusted)		PPI Finished Goods (seasonally adjusted)		PPI-Industrial Commodities (unadjusted)		Estimated GNP Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	118.5	118.5	108.3	108.3	106.7	106.8	121.9	122.0
August	119.0	119.0	108.9	108.9	107.1	107.1	122.2	122.3
September	119.4	119.4	109.3	109.3	106.9	106.9	122.7	122.8
October	119.9	119.9	109.2	109.5	107.2	107.1	123.0	123.3
November	120.4	120.3	109.4	109.8	107.5	107.4	123.3	123.7
December	120.8	120.8*	109.7	110.3*	107.8	108.1	123.6	124.1
January 1989	121.1	121.1	110.3	110.6	108.0	108.5	124.1	124.6
February	121.4	121.5	110.6	111.0	108.1	108.9	124.6	125.0
March	121.8	121.9	110.9	111.4	108.2	109.0	125.2	125.5
April	122.3	122.3	111.2	111.6	108.7	109.2	125.6	125.9
May	122.8	122.9	111.5	111.9	109.4	109.6	125.9	126.3
June	123.4	123.4	111.8	112.3	110.1	110.0	126.2	126.8
July	124.0	123.9	112.2	112.6	110.5	110.3	126.7	127.3
August	124.6	124.4	112.6	113.0	110.8	110.7	127.1	127.9
September	125.2	124.9	113.0	113.4	110.5	110.0	127.5	128.3
October	125.7	125.4	113.4	113.9	111.2	111.3	128.0	128.8
November	126.2	125.8	113.9	114.2	111.9	111.8	128.4	129.3
December	126.8	126.4	114.5	114.7	112.6	112.5	128.8	129.9

	Consumption Deflator		Consumer Durables		Consumer Nondurables		Consumer Services		Implicit Construction Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	124.8	124.8	110.1	110.0	116.9	116.9	135.1	135.1	116.0	116.0
August	125.1	125.1	110.4	110.4	117.1	117.0	135.5	135.5	115.9	115.9
September	125.7	125.8	110.6	110.6	117.9	117.9	136.1	136.2	116.1	116.4
October	126.2	126.4	110.8	111.0	118.2	118.3	136.7	136.8	116.3	116.6
November	126.6	126.8*	110.7	111.2*	118.5	118.7*	137.2	137.4*	116.5	116.6
December	127.0	127.2	110.9	111.4	118.9	119.2	137.8	138.0	116.7	116.9*
January 1989	127.4	127.7	111.2	111.6	119.2	119.6	138.5	138.6	116.8	117.1
February	127.9	128.1	111.5	111.8	119.5	120.0	139.0	139.1	117.0	117.3
March	128.4	128.6	111.8	112.1	119.8	120.4	139.5	139.7	117.2	117.4
April	129.0	129.0	112.0	112.3	120.5	120.7	140.1	140.3	117.4	117.6
May	129.8	129.6	112.0	112.5	121.3	121.1	140.8	141.0	117.4	117.7
June	130.0	130.1	112.2	112.7	122.0	121.6	141.5	141.6	117.6	117.9
July	130.7	130.6	112.5	113.0	122.3	122.1	142.0	142.3	117.8	118.1
August	131.1	131.2	112.9	113.3	122.6	122.7	142.6	142.9	118.1	118.4
September	131.4	131.7	113.3	113.5	122.9	123.1	143.2	143.5	118.4	118.6
October	132.1	132.2	113.5	113.8	123.6	123.6	143.8	144.1	118.6	118.8
November	132.6	132.7	113.4	114.1	124.2	124.2	144.4	144.7	118.8	119.1
December	133.1	133.3	113.6	114.4	124.8	124.8	145.0	145.3	119.0	119.3

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MISCELLANEOUS

	Merchandise Trade Balance		Leading Indicators		Estimated GNP		Estimated GNP (1982 $)		IVA (annual rate)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	-9.98	-9.98	192.7	192.4	4888	4891	4010	4009	-27.2	-28.6
August	-10.53	-10.53	193.4	193.4	4900	4906	4010	4011	-23.7	-30.4
September	-8.97	-8.57	193.6	192.8	4915	4930	4006	4015	-18.5	-33.3
October	-9.28	-8.88	194.2	193.6	4935	4959	4012	4022	-20.6	-27.4
November	-9.65	-10.18*	194.5	193.2	4954	4982	4018	4027	-21.9	-23.7
December	-10.02	-10.16	193.7	192.6*	4974	5007	4024	4035	-23.2	-25.6
January 1989	-8.76	-9.43	194.0	193.0	5016	5074	4042	4072	-16.5	-30.8
February	-7.93	-9.65	194.4	193.2	5066	5103	4066	4082	-14.8	-31.3
March	-7.39	-9.27	194.0	192.9	5107	5125	4079	4084	-13.0	-27.4
April	-7.05	-9.56	193.5	192.5	5127	5146	4082	4087	-17.6	-23.5
May	-7.38	-10.13	193.1	192.9	5148	5178	4089	4100	-19.9	-20.4
June	-7.34	-9.52	193.5	193.4	5169	5213	4096	4111	-22.3	-21.6
July	-8.21	-9.26	193.8	193.3	5194	5239	4099	4115	-22.1	-21.8
August	-8.46	-9.05	193.2	193.0	5221	5272	4108	4122	-22.6	-24.3
September	-8.65	-8.84	192.7	192.5	5248	5301	4116	4132	-23.1	-26.6
October	-7.73	-8.53	192.0	192.0	5279	5330	4124	4138	-26.9	-28.2
November	-7.27	-8.26	191.6	191.1	5301	5358	4129	4144	-28.0	-28.6
December	-6.80	-7.94	192.1	191.3	5323	5384	4133	4145	-29.1	-30.1

	Currency Index		Adjusted Profits		30-Year Government Bonds		New York Composite	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	96.53	96.53	191.2	187.2	9.14	9.14	152.12	152.12
August	98.29	98.29	188.5	185.4	9.32	9.32	149.25	149.25
September	97.91	97.91	183.7	183.0	9.06	9.06	151.47	151.47
October	94.63	95.10	173.5	186.4	9.01	8.89	157.63	156.36
November	90.46	91.91	166.7	187.9	9.17	9.02	160.26	152.67
December	87.01	92.65	160.5	184.3	9.30	9.01	160.63	155.83*
January 1989	85.56	93.15*	169.8	187.5	9.24	8.92*	161.25	163.73
February	88.42	91.26	173.8	189.2	9.26	8.73	162.29	167.21
March	91.26	91.02	177.7	190.5	9.25	8.66	162.05	165.14
April	92.15	89.65	175.2	190.3	9.30	8.72	154.43	165.26
May	90.45	87.43	173.8	188.1	9.33	8.89	149.62	163.68
June	91.03	86.11	172.5	186.4	9.52	9.06	145.15	166.25
July	91.72	84.23	174.0	186.7	9.65	9.24	143.65	162.43
August	92.43	85.46	174.9	184.5	9.54	9.49	152.43	163.72
September	93.06	86.62	173.6	182.3	9.59	9.67	153.11	158.65
October	92.20	86.29	169.4	180.1	9.73	9.72	149.25	155.27
November	89.25	85.53	167.8	180.8	9.88	9.70	147.85	153.52
December	86.93	84.95	166.2	178.5	10.03	9.71	142.25	150.46

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FINANCIAL MARKETS

	Monetary Base		M1		M2		Federal Funds		T-Bills (6 Mos.)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	280.3	280.2	782.4	782.3	3025.9	3025.8	7.75	7.75	6.99	6.99
August	281.1	281.1	782.5	782.5	3031.8	3031.6	8.01	8.01	7.36	7.36
September	282.1	282.3	782.5	782.3	3035.1	3034.1	8.19	8.19	7.43	7.43
October	284.0	283.3	785.3	783.5	3043.5	3037.5	8.25	8.30	7.36	7.50
November	285.3	285.0	792.6	783.6	3079.0	3054.0	8.23	8.35	7.37	7.76
December	286.6	285.0	799.3	787.5	3106.5	3066.2	8.22	8.76	7.37	8.24
January 1989	288.4	288.1*	803.1	794.6*	3120.4	3078.9*	8.20	9.02*	7.35	8.38*
February	290.2	289.3	805.3	797.9	3134.5	3090.5	8.18	9.06	7.36	8.41
March	291.9	290.6	807.6	801.8	3148.6	3106.0	8.22	9.11	7.37	8.37
April	293.7	291.9	811.9	805.1	3167.7	3121.5	8.24	9.16	7.40	8.34
May	295.0	293.3	817.7	808.8	3188.6	3140.2	8.25	9.08	7.46	8.29
June	296.3	295.0	823.2	813.3	3208.9	3160.7	8.35	9.22	7.55	8.42
July	298.0	296.7	826.9	818.2	3229.3	3183.6	8.33	9.37	7.52	8.59
August	299.5	298.2	831.4	822.1	3249.1	3202.7	8.30	9.56	7.40	8.73
September	300.9	299.6	834.9	826.0	3268.8	3221.8	8.36	9.73	7.42	8.85
October	302.5	301.1	838.6	830.0	3281.4	3241.1	8.55	9.89	7.69	8.99
November	304.3	302.4	842.9	833.4	3299.1	3257.3	8.92	9.96	7.89	9.13
December	306.0	303.7	847.3	836.7	3317.6	3276.8	9.03	9.93	8.01	9.20

	Aaa (Seasoned)		Municipals (Bond Buyer)		(3 Month) Commercial Paper		90 Day CD's		Prime Rate	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
July 1988	9.96	9.96	7.76	7.76	7.82	7.82	7.94	7.94	9.29	9.29
August	10.11	10.11	7.79	7.79	8.26	8.26	8.35	8.35	9.84	9.84
September	9.82	9.82	7.66	7.66	8.17	8.17	8.23	8.23	10.00	10.00
October	9.68	9.51	7.49	7.47	8.23	8.24	8.30	8.36	10.00	10.00
November	10.01	9.45	7.80	7.46	8.24	8.66	8.32	8.78	10.00	10.05
December	10.17	9.57	7.85	7.61	8.29	9.11	8.38	9.25	10.00	10.50
January 1989	10.05	9.63*	7.82	7.43*	8.25	9.02*	8.33	9.18*	10.00	10.50
February	10.08	9.61	7.83	7.40	8.26	8.96	8.35	9.12	10.00	10.50
March	10.10	9.58	7.87	7.36	8.24	8.95	8.33	9.09	10.00	10.50
April	10.15	9.65	7.92	7.43	8.27	9.06	8.40	9.20	10.00	10.86
May	10.20	9.84	7.95	7.59	8.30	9.03	8.41	9.16	10.00	11.00
June	10.24	10.01	7.98	7.75	8.37	9.27	8.46	9.38	10.00	11.00
July	10.33	10.23	8.04	7.93	8.39	9.43	8.50	9.53	10.00	11.00
August	10.38	10.36	8.08	8.01	8.42	9.62	8.56	9.72	10.00	11.34
September	10.45	10.49	8.15	8.10	8.45	9.80	8.60	9.91	10.00	11.50
October	10.62	10.55	8.31	8.13	8.66	9.95	8.73	10.04	10.46	11.72
November	10.73	10.51	8.40	8.10	9.03	9.92	9.15	10.02	10.75	12.00
December	10.82	10.53	8.46	8.06	9.15	9.90	9.26	10.00	11.00	12.00

Fore. = November Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

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ECONOMIC FORECASTING CENTER

MONTHLY PROJECTIONS
January 1989

Dr. Donald Ratajczak, Director
For Release: February 24, 1989

WEATHER HAS CREATED A JANUARY EFFECT

Many investors are aware that tax-loss selling toward the end of the year leads to decreases in values of over-the-counter stocks, which are heavily held by individual investors. In the beginning of a new year, the selling subsides and some of these issues are repurchased. As a result, the stock market tends to rise, led by smaller valuation issues. Such a condition occurred this January. This phenomenon has become known as the "January Effect".

Unusually mild weather in January apparently is creating another January Effect. Economic data has appeared more robust than anticipated. In addition, the beginning of year shifting of weights and changing seasonal adjustments has created the appearance of sharply accelerating inflation. Combined, these events suggest that a resurgence in economic activity developed.

Such a resurgence will not be certain until the data for February becomes available. If the mild weather created a "January Effect" in the economic data, January's robust readings will be followed by exceptionally sluggish growth in February. This is what is anticipated as winter weather reappeared in that month.

Indeed, the weather-related distortions in January probably were widespread. Not only was there the obvious acceleration in housing activity because so much work could be accomplished, but the absence of any weather-delaying conditions probably aided retail activity, except in the apparel area, and even manufacturing.

However, not all January data appears to have been significantly improved by this mild weather. Excluding utilities, industrial production showed a spurt of 0.5%, but the warm weather clearly reduced the demand for utilities. As a result, total industrial production rose only 0.3%. This led to no change in measured capacity utilization, even though the utilization rates of factories rose 0.2 percentage points.

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While mild weather distorted economic conditions, President Bush was able to propose adjustments to the Reagan budget that appeared to please everybody, except those who wanted to see attempts to reduce budget deficits. The President introduced several new programs, including tax exemptions for enterprise zones, child care, and capital gains. The capital gains provision is not expected to become law.

Unfortunately, the Bush projections of less than $100 billion in deficits in the next fiscal year are based upon faulty economic assumptions. The budget assumes that short-term interest rates will average 7% this year. That appears to be 2 percentage points too low. Deficits probably will increase approximately $6 billion for every percentage point error in interest rate estimates.

Also, economic growth probably is overstated by about 0.5 percentage points. This causes several billion more in overstated revenues. The Bush budget also continues overestimating corporate profit tax collections. Corporate restructuring clearly has been a factor in sharply reducing effective corporate tax rates. Another $10 billion in overestimated revenues probably occurred here. Provisions for the savings and loan bailout are not fully reflected. More than $50 billion in bonds will be issued this year to support shaky assets in that industry. They will be counted as investments by the insurance agency. Interest paid on those bonds over and above any increased insurance premium will reflect an agency loss. Therefore, deficits of government enterprises probably will be $7 billion higher than currently projected. While some budgetary savings will occur as Congress reduces defense below even zero real growth, increases in other expenditures probably will wash out. The result is probably a deficit that is underestimated by $35 billion.

Of course, even though long-term government bonds used to finance S&L assets will not be included in the deficit, they will be an increased burden upon the long-term bond market. For that reason, long-term interest rates are expected to rise further. Bush's budget and the S&L problems almost assure rising interest rates through most of the year.

Quarterly Profile of GNP

	1988-4	1989-1	1989-2	1989-3	1989-4	1990-1	1988 Annual	1989 Annual
Real:	2.0	5.0	3.3	2.3	1.5	1.2	3.8	2.9
Price:	4.7	4.3	4.7	5.2	5.4	5.3	3.3	4.6
Nominal:	6.8	10.1	8.2	7.8	7.0	7.0	7.3	7.7

Monthly Statistical Highlights

	January 1989	February 1989
Payroll Employment		+168,000
Index of Hours Worked		+0.2%
Household Employment		+165,000
Civilian Unemployment Rate		5.4%
Personal Income	+0.8%	+0.7%
Retail Sales		+0.9%
Auto Sales		10.0 *
Housing Starts		+12.4%
Housing Permits		-3.9%
Savings Rate	5.0%	
Personal Consumption	+0.4%	
Construction Expenditures	+1.2%	-2.8%
Business Inventories	+0.6%	+0.6%
Orders For Durable Goods	-4.7%	-0.2%
Orders For Nondefense Capital Goods	-8.2%	-1.7%
Industrial Production		+0.3%
CPI		+0.3%
PPI		+0.4%
Consumption Deflator	+0.4%	+0.4%
Leading Indicators	-0.2%	-0.3%
Currency Index		+1.1%
Equity Index		+2.1%
Real GNP (AR)	+5.8%	+0.3%
M1 (AR)		+4.0%
M2 (AR)		+3.7%

* auto sales in millions

Commentary

Employment - Employment was exceptionally strong in January as construction increased by more than 100,000 and manufacturing activity was up more than 35,000. Strong gains in retail activity also suggest that weather probably unduly stimulated activity there as well. The index of hours worked surged by 1%. Obviously, a continuation of strong employment growth would imply dramatic first-quarter increases in real GNP. However, the absence of inclement weather may have overstated payroll employment by more than 150,000. This would suggest that underlying employment probably was growing 250,000. With some absence of growth in those sectors during February, unusually modest employment growth is expected at that time. An extension of the workweek may also reflect the absence of inclement weather. Therefore, the workweek should shrink next month.

The surge in civilian employment is more difficult to explain. Perhaps, the surveys merely are catching up with the enormous overstatement of payroll employment that occurred during 1988.

Instead of the hourly earnings index, it is now necessary to rely upon hourly earnings, which are not adjusted for overtime and composition shifts. As overtime increased in January, the 0.6% increase in hourly earnings probably overstates wage pressures. Nevertheless, some intensifying wage pressures probably are developing. Following compensation increases of 5.8% in the third quarter and 5.7% in the fourth quarter, compensation may have increased more than 6% in the first quarter of 1989. Initial unemployment claims are gradually drifting upward, although the weekly fluctuations have widened. This confirms our belief that economic activity probably was relatively sluggish during the month.

Personal Income and Outlays - Sharp increases in hourly earnings and in payrolls suggest that the wage component of personal income grew sharply. In addition, farm income remains sharply depressed. With shifts in estimated farm inventory holdings early in 1989 as a result of the ending of the drought effect, personal income should surge sharply during the first quarter. This will lead to higher estimated savings rates. Although retail sales did not capture the surge followed by slump in units sold, the durable goods component of personal outlays did. Because of a sharp surge in December, a significant slowing is expected in durable expenditures in January. Price increases probably will lead to a significant spurt in nondurables. In addition, increasing stock market activity suggests that the service component also will be growing sharply. This suggests that real consumer spending will not retrench in January following sharp gains in December.

Failure of automobile sales to reflect fluctuations in unit auto sales remains a mystery. Perhaps, a significant upward adjustment in auto sales will develop when annual adjustments to the survey are made. Sales of nonauto durables have been surprisingly strong, but this probably is reflected by weather conditions. The remodeling market has been unusually brisk for this time of year. Indeed, some slowing might develop in nonauto durables during February when winter returns.

Construction - Better weather appears to be more important in generating housing activity than higher mortgage rates are responsible for dampening it. However, a decline in housing permits during January despite an 8% surge in housing starts strongly suggests that temporary weather conditions are completely responsible for the strong housing sector. As weather reversed direction in February, a significant drop is expected in housing activity. Furthermore, continuing increases in interest rates suggest that housing will weaken further in the spring.

Weather clearly assured strong growth in consumer spending in December. A continuation of that favorable weather will probably add to spending programs in January. However, public construction almost certainly will drop off sharply following that month. Nonresidential activity also should be slated for a significant decline.

Inflation increased a little for construction materials in December. However, no substantial inflationary pressures appear in that sector at this time.

Business Activity - Commercial aircraft continues to be a significant factor in stimulating nondefense capital goods orders. Orders were up dramatically in December both as a result of aircraft orders, strong automobile deliveries, and strong military orders. The military certainly should be reversed next month, as it was heavily dependent upon significant naval ship deliveries. However, capital goods orders are far outstripping capital shipments at the present time. This suggests that stronger capital spending probably is in store for much of 1989.

Business inventories remain modest. Sluggish retail sales in December caused a spurt in retail inventories, but they had been well-managed in previous months. Manufacturing inventories are beginning to spurt, but no substantial imbalances in any inventory sectors appears at the present time.

Industrial production probably was overstated in the factory sector as a result of favorable weather. On the other hand, utilities were unusually low. In February, this pattern should reverse, with a continuation of modest growth in both industrial production and capacity utilization. Despite some upward revisions in capacity estimates, capacity continues to grow as measured by the Federal Reserve by only 2.5% per year.

Prices - Inflation reappeared in January. A large increase in fees for entertainment and hospitals caused a 6% annual rate of growth in the service sector. Although some January pricing patterns may have accelerated those adjustments at this time, higher wages and expectations of increasing inflation clearly also are factors. This suggests that consumer prices probably will grow more rapidly than originally expected, at least in the early months of this year.

On the other hand, a 1.0% increase in the PPI was partially the result of significant seasonal adjustment distortions. In making their annual seasonal adjustments, the Bureau of Labor Statistics assumed that the OPEC-induced price declines in 1986 and 1987 reflected normal seasonal behavioral patterns. A more appropriate procedure would have removed those observations as clearly being exogenous. The result was a 0.4% upward adjustment in the PPI seasonal for January. The seasonal in February will be adjusted upward by 0.2 percentage points from the previous year while March will be adjusted downward by 0.2 percentage points. Thus, after growing very rapidly in December and January, the PPI could grow very slowly or not at all by March.

These sharp increases in prices will lead to more rapid growth in the GNP deflator than previously expected. Inflation as measured by the CPI probably will grow between 5.0% and 5.5% in 1989. The GNP deflator probably will now grow between 4.5% and 5%.

Miscellaneous - Despite a 6% increase in exports during December, the trade deficit showed minimal improvement. Sharp increases in oil imports were partially responsible for this disappointing result. However, the value of oil will continue to rise as higher priced oil is delivered in January and February. In addition, exports should not grow so robustly in the next few months. Indeed, merchandise trade balances are hovering near $10 billion a month after improving significantly in the past year.

Part of this disappointing improvement clearly is the result of continued strength in the dollar's value. Anticipations of higher interest rates in the United States along with belief that currency stability will be maintained has led to a stronger dollar against some of the leading currencies. However, failure to register further improvement in the merchandise trade balances almost certainly will lead to dollar declines as the year progresses.

The sharp increase in prices will cause real money balances to fall in January. Also, slow permit growth indicates the leading indicators may decline slightly.

However, stronger growth in economic activity, even if it is the result of unusual weather, should lead to greater profitability. This, in turn, appears to be a factor supporting higher equity values. When interest rates rise, the dollar falls, and declining growth rates lead to falling profitability, equity values should decline. Our current projections show a decline developing in the spring.

Financial Markets

Strong farm income should add to household savings early in the year. As a result, the household sector could be encouraging slight declines in interest rates. Later in the year, however, slower employment growth should restrict the capacity of the household sector to significantly increase savings behavior.

More significant interest rate pressures will be developing from the corporate sector. Borrowings are expected to remain heavy through the year as capital expansion and inventory accumulation exceed cash flow. Any acceleration of inflationary pressures will merely add to the borrowing needs for inventory investment purposes.

Government borrowings will remain relatively stable through the year. This suggests that the deficit will neither be declining nor rising through most quarters.

Thus, domestic savings flows would suggest some gradual increases in interest rates as a result of corporate borrowings slightly exceeding household net additions to savings.

As has been the case in recent months, the direction of interest rates will depend heavily upon the expectations of foreign investors. As long as those investors believe that the dollar can remain stable, positive capital flows will prevent interest rates from rising. However, once the dollar begins sliding and generating anticipations that further declines are likely higher interest rates will be necessary to entice foreign capital flows. This dollar weakness is expected to begin surfacing as early as late February. Thus, some upward pressures upon interest rates could be developing at that time.

At the same time, the Federal Reserve is engaging in monetary restraint. This restraint is generating higher interest rate pressures. Clearly, rising inflationary pressures suggest that restraint will persist through most of 1989. Only late in the year will a possible reversal of tight monetary restraint be possible. Thus, interest rates could begin trending down late this year or early next year. In the meantime, sharply higher interest rates appear in store.

Equity Markets - As long as interest rates remain stable, growth generates increasing profitability, and the dollar remains strong, equity values will increase. When those conditions turn, as they have done temporarily late in February, equity values will decline. However, interest rates should again stabilize and even decline slightly in the next month or so. The dollar should remain near current levels. However, the Dow Jones is not expected to rise significantly above 2300 in a spring advance. Moreover, a decline to the vicinity of 2000 appears likely by the end of the year.

EMPLOYMENT

	Payroll Employment		Index of Hours Worked		Household Civilian Employment		Civilian Unemployment Rate		Hourly Earnings	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	106973	106973	127.1	127.1	115573	115573	5.3	5.3	9.43	9.43
November	107377	107419	127.0	127.1	115947	115947	5.4	5.4	9.42	9.42
December	107656	107640	127.1	127.2	116009	116009	5.3	5.3	9.44	9.44
January 1989	108026	108048	127.6	128.5	116435	116711	5.3	5.4	9.50	9.50
February	108277	108216*	128.0	128.2*	116700	116876*	5.2	5.4*	9.55	9.54*
March	108526	108473	128.4	128.5	116965	117142	5.2	5.3	9.60	9.59
April	108753	108729	128.7	128.9	117168	117423	5.1	5.2	9.63	9.62
May	108960	108993	129.0	129.2	117381	117714	5.0	5.1	9.66	9.65
June	109165	109176	129.2	129.3	117592	117902	5.0	5.2	9.68	9.69
July	109328	109355	129.4	129.5	117746	118098	5.0	5.2	9.72	9.73
August	109555	109562	129.7	129.7	117980	118334	5.0	5.1	9.77	9.78
September	109784	109759	129.9	130.0	118221	118484	4.9	5.2	9.81	9.82
October	109938	109962	130.0	130.2	118403	118705	4.9	5.1	9.85	9.87
November	110037	110143	130.2	130.3	118559	118919	4.9	5.1	9.90	9.93
December	110235	110352	130.3	130.5	118716	119148	4.9	5.0	9.95	9.99
January 1990	110423	110517	130.6	130.7	118914	119333	4.8	4.9	9.99	10.04
February	110617	110703	130.8	130.9	119151	119550	4.8	4.9	10.04	10.10
March	110809	110886	131.1	131.1	119362	119788	4.9	4.9	10.09	10.16

PERSONAL INCOME

	Personal Income		Wage & Salary		Personal Savings		Disposable Income		Personal Outlays	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	4.184	4.178	2.512	2.508	182.9	178.8	3.587	3.583	3.404	3.404
November	4.175	4.170	2.520	2.516	153.3	156.5	3.577	3.573	3.423	3.416
December	4.196	4.207	2.522	2.530	157.6	158.5	3.598	3.606	3.440	3.448
January 1989	4.223	4.242*	2.543	2.562*	167.9	181.8*	3.620	3.643*	3.452	3.461*
February	4.272	4.273	2.571	2.577	189.6	187.4	3.664	3.673	3.474	3.486
March	4.320	4.310	2.599	2.601	206.3	194.5	3.702	3.708	3.496	3.514
April	4.343	4.340	2.608	2.617	200.6	195.6	3.719	3.734	3.518	3.538
May	4.366	4.363	2.617	2.632	196.7	198.6	3.734	3.752	3.537	3.553
June	4.389	4.388	2.626	2.645	197.3	193.7	3.750	3.770	3.553	3.576
July	4.412	4.411	2.645	2.661	197.1	193.1	3.773	3.786	3.576	3.593
August	4.434	4.439	2.665	2.679	199.8	200.0	3.797	3.808	3.597	3.608
September	4.456	4.467	2.686	2.697	201.8	198.6	3.820	3.830	3.618	3.631
October	4.479	4.495	2.699	2.715	195.3	205.3	3.835	3.850	3.640	3.645
November	4.501	4.526	2.712	2.735	192.7	206.9	3.852	3.874	3.659	3.667
December	4.523	4.557	2.725	2.756	191.1	210.1	3.868	3.899	3.677	3.689
January 1990	4.552	4.577	2.744	2.775	194.2	212.8	3.895	3.924	3.701	3.711
February	4.582	4.607	2.764	2.796	202.5	213.9	3.926	3.942	3.724	3.728
March	4.613	4.639	2.785	2.818	209.4	221.8	3.953	3.971	3.744	3.749

Fore. = February Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

CONSUMPTION

	Personal Consumption		Durables		Nondurables		Services		Consumption Real	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	3302.9	3302.2	452.0	452.0	1071.3	1071.3	1778.8	1778.8	2613.6	2612.5
November	3321.6	3313.7	453.6	453.6	1077.4	1077.4	1782.6	1782.6	2617.9	2617.9
December	3335.8	3344.5	472.1	472.1	1076.9	1076.9	1795.5	1795.5	2635.4	2635.4
January 1989	3349.1	3358.2*	460.7	464.4*	1080.5	1085.5*	1807.6	1808.3*	2628.8	2635.2*
February	3371.0	3382.2	463.5	470.6	1085.6	1090.1	1821.9	1821.5	2637.7	2643.5
March	3391.9	3409.7	466.5	480.3	1090.8	1095.4	1834.6	1834.3	2643.7	2655.8
April	3414.1	3434.1	470.2	487.5	1097.4	1098.7	1846.5	1847.9	2646.6	2664.5
May	3432.5	3448.6	472.4	483.8	1101.3	1104.1	1858.5	1860.7	2648.5	2663.3
June	3447.4	3471.0	471.6	487.5	1105.5	1109.3	1870.3	1874.2	2647.8	2668.9
July	3470.1	3487.1	474.3	485.2	1113.4	1115.4	1882.4	1886.5	2655.0	2670.1
August	3490.9	3501.7	476.8	481.4	1118.6	1120.6	1895.5	1899.7	2662.8	2669.8
September	3511.4	3524.6	479.3	486.4	1123.9	1126.0	1908.2	1912.2	2670.3	2677.1
October	3532.3	3537.3	481.5	481.6	1130.1	1131.6	1920.7	1924.1	2671.9	2674.0
November	3551.1	3558.9	483.3	484.4	1134.0	1136.9	1933.8	1937.6	2672.0	2677.3
December	3567.9	3579.9	483.3	488.0	1138.0	1141.4	1946.6	1950.5	2672.6	2680.2
January 1990	3591.6	3601.8	486.5	489.9	1146.2	1149.1	1958.9	1962.8	2680.3	2685.1
February	3614.0	3618.3	489.4	490.0	1151.9	1154.0	1972.7	1974.3	2687.0	2685.7
March	3633.8	3638.9	490.2	490.7	1157.5	1160.7	1986.3	1987.5	2691.7	2688.8

RETAIL SALES

	Retail Sales		Non-Auto Durables		Auto (Million Units)		Nondurable Sales		Auto Sales	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	136.56	136.56	20.90	20.90	9.8	9.9	85.36	85.36	30.30	30.30
November	137.81	137.87	21.10	21.10	10.2	10.2	85.80	85.80	30.91	30.91
December	138.03	138.15	21.51	21.69	11.7	11.6	85.70	85.78	30.82	30.69
January 1989	138.04	138.91	21.27	22.04	9.9	9.8	86.04	86.47	30.73	30.40
February	138.77	140.15*	21.16	22.30*	10.3	10.0*	86.45	86.83*	31.16	31.02*
March	139.52	141.68	21.13	22.36	10.7	10.5	86.86	87.26	31.53	32.06
April	140.47	142.75	21.58	22.50	10.6	10.7	87.39	87.52	31.50	32.73
May	141.03	142.77	21.57	22.27	10.7	10.6	87.70	87.95	31.76	32.55
June	141.27	143.59	21.65	22.43	10.6	10.7	88.03	88.36	31.59	32.80
July	141.50	143.82	21.88	22.61	10.2	10.5	88.66	88.85	30.96	32.36
August	142.90	143.80	22.24	22.80	10.5	10.3	89.08	89.26	31.58	31.74
September	143.60	144.80	21.99	22.76	10.8	10.5	89.50	89.69	32.11	32.35
October	144.34	144.70	22.38	23.04	10.1	10.2	89.99	90.14	31.97	31.52
November	144.86	145.44	22.23	23.20	10.3	10.4	90.30	90.56	32.33	31.68
December	145.18	146.21	21.80	22.86	10.6	10.7	90.62	90.92	32.76	32.43
January 1990	146.19	147.03	22.33	22.95	10.5	10.6	91.27	91.53	32.59	32.55
February	146.97	147.44	22.56	23.11	10.6	10.5	91.73	91.92	32.68	32.41
March	147.49	148.06	22.70	23.05	10.5	10.5	92.17	92.46	32.62	32.55

Fore. = February Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

CONSTRUCTION

	Housing Starts		Single Family Starts		Housing Permits		Construction Expenditures (Current)		Construction Expenditures (Real)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	1.542	1.533	1.112	1.136	1.516	1.516	407.8	408.2	349.8	350.1
November	1.563	1.558	1.151	1.135	1.517	1.516	411.1	412.4	352.6	353.7
December	1.506	1.568	1.121	1.123	1.502	1.566	408.2	422.7	349.2	361.6
January 1989	1.490	1.693	1.095	1.203	1.473	1.523	410.3	427.8*	350.4	365.4*
February	1.443	1.483*	1.063	1.083*	1.416	1.463*	409.8	416.5	349.7	355.1
March	1.405	1.466	1.032	1.076	1.372	1.442	409.4	416.7	348.7	354.4
April	1.457	1.478	1.056	1.075	1.375	1.443	409.3	411.0	348.0	348.9
May	1.490	1.460	1.084	1.062	1.413	1.427	409.5	411.0	347.3	348.0
June	1.466	1.467	1.055	1.054	1.392	1.416	409.3	411.5	346.6	347.5
July	1.438	1.447	1.037	1.036	1.375	1.392	411.9	411.2	347.9	346.4
August	1.414	1.432	1.025	1.021	1.356	1.376	413.2	411.2	347.8	345.3
September	1.423	1.417	1.011	1.002	1.364	1.343	414.4	409.5	347.7	342.9
October	1.425	1.398	1.020	0.993	1.343	1.345	414.3	408.8	346.7	341.5
November	1.413	1.388	1.012	0.976	1.327	1.336	414.6	407.2	346.1	339.3
December	1.414	1.395	1.018	0.984	1.330	1.343	414.5	408.1	344.8	339.3
January 1990	1.369	1.406	0.984	0.992	1.306	1.348	414.9	409.5	344.0	339.6
February	1.358	1.407	0.976	1.005	1.298	1.350	416.1	412.8	343.9	341.1
March	1.345	1.424	0.968	1.008	1.299	1.358	417.4	416.1	343.5	342.7

	Non-Residential		Public Construction		Residential Construction	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	130.9	130.7	77.9	77.9	199.0	199.6
November	129.7	131.6	80.9	80.5	200.4	200.3
December	128.4	135.3	79.5	86.8	200.3	200.9
January 1989	128.8	136.0*	81.0	86.5*	200.5	205.3*
February	128.4	131.6	80.6	82.5	200.8	202.4
March	127.8	132.0	81.5	82.7	200.1	202.0
April	128.3	130.9	81.7	82.5	199.3	197.6
May	128.8	130.5	82.0	82.9	198.7	197.6
June	129.2	130.1	82.0	83.2	198.1	198.2
July	129.5	130.4	82.5	83.0	199.9	197.8
August	129.8	130.1	82.6	83.4	200.8	197.7
September	130.1	129.7	82.8	83.3	201.5	196.5
October	130.4	129.9	83.0	83.7	200.9	195.2
November	130.6	129.5	83.2	83.5	200.8	194.2
December	130.9	130.1	82.8	83.9	200.8	194.1
January 1990	131.5	129.6	83.5	84.4	199.9	195.5
February	132.3	130.5	84.2	84.7	199.6	197.6
March	133.1	131.3	84.9	85.2	199.4	199.6

Fore. = February Forecast
C.E. = Current Expectations
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BUSINESS ACTIVITY

	Manufacturers' Inventories		Durable Goods Orders		Non-Defense Capital Goods Orders		Non-Defense Capital Shipments	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	349.4	349.4	122.79	122.79	34.62	34.62	32.69	32.60
November	350.9	351.6	122.77	123.04	35.67	35.83	32.43	32.51
December	352.4	354.0	121.85	130.95	34.23	38.75	32.47	32.34
January 1989	354.3	356.3*	123.74	124.76*	34.93	35.56*	32.96	32.63*
February	356.8	358.2	122.19	124.55	33.67	34.95	33.02	32.85
March	359.2	360.1	122.85	124.92	33.84	35.17	33.10	33.26
April	361.5	362.3	123.75	125.16	34.26	34.73	33.43	33.49
May	363.6	364.5	123.14	125.89	34.05	34.92	33.88	33.72
June	365.8	366.7	123.67	126.39	34.35	35.14	34.25	33.94
July	367.9	368.5	124.51	127.01	34.97	34.85	34.56	34.26
August	369.5	370.9	125.89	127.25	35.37	34.96	34.65	34.53
September	372.3	373.5	125.11	126.54	35.11	35.21	34.47	34.29
October	374.6	375.7	124.48	126.82	34.96	34.85	34.69	34.36
November	376.8	378.1	125.93	127.73	35.22	34.72	34.83	34.72
December	378.9	380.4	126.21	127.65	35.29	34.53	34.98	35.03
January 1990	381.1	383.6	127.72	128.82	35.56	34.59	35.15	35.13
February	382.4	385.9	127.85	127.91	36.42	34.65	35.70	34.89
March	383.7	387.1	127.56	128.12	36.40	34.63	36.28	35.27

	Business Inventories		Defense Shipments		Industrial Production		Capacity Utilization	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	751.4	750.6	8.43	8.43	139.3	139.4	84.0	84.0
November	754.4	753.7	8.55	8.66	139.9	139.9	84.2	84.1
December	755.0	760.6	8.63	10.10	140.2	140.6	84.1	84.4
January 1989	760.6	765.3*	8.54	8.73*	140.8	141.1	84.3	84.4
February	766.5	770.1	8.51	8.65	141.2	141.5*	84.4	84.5*
March	772.3	775.2	8.43	8.67	141.6	141.9	84.5	84.6
April	775.7	779.7	8.50	8.48	142.3	142.4	84.8	84.8
May	779.6	783.8	8.55	8.59	142.7	142.8	84.9	84.9
June	783.4	787.5	8.56	8.62	143.2	143.3	85.1	85.1
July	788.1	792.4	8.53	8.65	143.4	143.6	85.0	85.1
August	792.0	797.3	8.55	8.72	143.2	143.9	84.7	85.1
September	795.8	803.1	8.56	8.78	143.5	144.1	84.7	85.0
October	801.1	808.2	8.59	8.69	143.7	144.4	84.6	85.0
November	806.6	813.1	8.61	8.76	143.8	144.7	84.5	85.0
December	812.1	818.9	8.63	9.42	143.9	145.0	84.4	85.0
January 1990	815.3	824.1	8.60	8.57	144.1	145.2	84.3	84.9
February	818.2	829.3	8.65	8.73	144.3	145.4	84.2	84.8
March	821.1	833.7	8.73	8.72	144.6	145.5	84.2	84.7

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PRICES

	CPI-U (seasonally adjusted)		PPI Finished Goods (seasonally adjusted)		PPI-Industrial Commodities (unadjusted)		Estimated GNP Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	119.9	119.9	109.5	109.5	107.1	107.1	123.4	123.4
November	120.3	120.3	109.8	109.8	107.4	107.4	123.8	123.8
December	120.8	120.7	110.3	110.2	108.1	108.1	124.2	124.1
January 1989	121.2	121.3	110.8	111.3	108.7	109.1	124.5	124.7
February	121.5	121.7*	111.1	111.7*	109.0	109.4*	124.8	125.2
March	121.8	122.1	111.4	111.9	109.1	109.8	125.1	125.6
April	122.4	122.5	111.8	112.4	109.7	110.1	125.6	126.0
May	122.9	123.0	112.1	112.8	110.2	110.4	126.1	126.4
June	123.3	123.6	112.4	113.2	110.6	111.0	126.5	126.9
July	124.0	124.1	112.8	113.5	111.3	111.4	127.0	127.3
August	124.7	124.6	113.3	113.8	111.8	111.8	127.4	127.8
September	125.4	125.2	113.9	114.2	110.5	110.5	127.8	128.2
October	125.9	125.8	114.4	114.6	111.8	112.1	128.4	128.7
November	126.3	126.3	114.8	115.1	112.1	112.5	128.9	129.2
December	126.7	126.9	115.1	115.5	112.4	112.7	129.5	129.8
January 1990	127.3	127.4	115.6	115.9	113.0	113.2	129.9	130.3
February	127.9	128.0	116.3	116.4	113.6	113.7	130.3	130.9
March	128.5	128.6	117.0	117.0	114.1	114.3	130.7	131.5

	Consumption Deflator		Consumer Durables		Consumer Nondurables		Consumer Services		Implicit Construction Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	126.4	126.4	111.0	111.0	118.4	118.4	136.8	136.8	116.6	116.6
November	126.6	126.6	111.1	111.1	118.2	118.2	137.3	137.3	116.6	116.6
December	126.9	126.9	111.8	111.8	118.4	118.4	137.8	137.8	116.9	116.9
January 1989	127.4	127.4*	112.0	112.4*	118.6	118.7*	138.4	138.3*	117.1	117.1*
February	127.8	127.9	112.3	112.7	118.7	119.2	138.9	138.9	117.2	117.3
March	128.3	128.4	112.6	113.0	119.4	119.6	139.3	139.5	117.4	117.6
April	129.0	128.9	112.9	113.2	120.2	120.1	140.0	140.1	117.6	117.8
May	129.6	129.5	113.1	113.5	120.9	120.6	140.8	140.8	117.9	118.1
June	130.2	130.1	113.3	113.8	121.5	121.1	141.5	141.5	118.1	118.4
July	130.7	130.6	113.7	114.1	121.8	121.6	142.1	142.1	118.4	118.7
August	131.1	131.2	114.1	114.4	122.0	122.1	142.7	142.7	118.8	119.1
September	131.5	131.7	114.5	114.6	122.3	122.5	143.3	143.4	119.2	119.4
October	132.2	132.3	114.8	115.0	123.0	123.0	144.0	144.1	119.5	119.7
November	132.9	132.9	115.1	115.3	123.8	123.7	144.7	144.8	119.8	120.0
December	133.5	133.6	115.4	115.6	124.6	124.4	145.4	145.5	120.2	120.3
January 1990	134.0	134.1	115.7	116.0	124.9	125.0	146.0	146.1	120.6	120.6
February	134.5	134.7	116.0	116.3	125.1	125.5	146.7	146.8	121.0	121.0
March	135.0	135.3	116.3	116.6	125.4	126.1	147.4	147.5	121.5	121.4

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MISCELLANEOUS

	Merchandise Trade Balance		Leading Indicators		Estimated GNP		Estimated GNP (1982 $)		IVA (annual rate)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	-8.88	-8.88	193.6	193.6	4963	4963	4022	4022	-24.4	-24.4
November	-10.18	-10.38	193.2	193.2	4984	4984	4026	4026	-20.7	-20.7
December	-9.96	-9.96	192.6	194.4	5023	5023	4044	4048	-20.6	-20.6
January 1989	-10.26	-10.17*	193.0	194.0*	5066	5072	4069	4067	-20.1	-23.9
February	-10.72	-10.29	193.2	193.5	5085	5093	4075	4068	-21.4	-26.4
March	-10.35	-9.58	192.9	194.2	5120	5128	4093	4083	-22.7	-27.8
April	-10.11	-9.93	192.5	194.5	5153	5157	4103	4093	-21.9	-24.3
May	-10.01	-10.25	192.9	194.1	5186	5189	4113	4105	-21.5	-21.2
June	-9.86	-9.82	193.4	192.7	5219	5225	4126	4117	-21.3	-19.8
July	-9.95	-9.95	193.3	193.1	5237	5249	4124	4123	-25.9	-20.5
August	-9.81	-9.76	193.0	193.5	5258	5273	4127	4142	-28.3	-24.6
September	-9.65	-9.53	192.5	193.8	5279	5298	4131	4133	-31.0	-28.1
October	-9.55	-9.48	192.0	192.8	5305	5335	4132	4145	-27.6	-29.2
November	-9.94	-9.97	191.1	192.5	5334	5376	4138	4161	-25.3	-30.6
December	-10.28	-10.11	191.3	193.0	5362	5403	4141	4163	-23.1	-29.5
January 1990	-9.79	-9.83	190.7	193.2	5390	5442	4149	4177	-29.6	-27.3
February	-9.71	-9.51	190.9	193.6	5417	5467	4157	4176	-31.3	-25.6
March	-9.64	-9.27	190.5	193.1	5445	5498	4166	4181	-33.0	-25.9

	Currency Index		Adjusted Profits		30-Year Government Bonds		New York Composite	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	95.10	95.10	185.4	185.4	8.89	8.89	156 36	156.36
November	91.91	91.91	186.9	186.9	9.02	9.02	152.67	152.67
December	92.65	91.88	177.3	180.3	9.01	9.01	155.34	155.34
January 1989	95.43	95.12	182.2	186.3	8.92	8.93	158.53	158.26
February	97.22	96.14*	181.1	182.5	9.03	9.04*	161.46	161.53*
March	96.25	95.73	179.9	184.2	9.04	9.06	161.06	161.92
April	94.43	94.58	178.5	182.7	8.86	8.91	163.49	164.85
May	93.36	92.75	177.2	183.9	8.73	8.87	162.25	165.27
June	92.71	94.26	175.8	185.3	9.02	9.11	158.07	162.36
July	92.43	94.20	171.2	180.7	9.38	9.43	154.62	157.53
August	92.00	92.73	169.3	181.6	9.53	9.52	151.72	154.48
September	91.66	91.55	167.6	179.5	9.51	9.60	148.85	156.69
October	90.43	90.22	166.8	173.2	9.63	9.55	150.25	153.82
November	86.55	88.77	165.5	171.8	9.69	9.64	149.53	150.91
December	86.92	86.29	164.5	172.3	9.83	9.73	148.86	149.76
January 1990	90.43	86.85	160.2	170.1	9.80	9.72	145.79	148.95
February	91.67	87.82	156.5	168.4	9.79	9.75	144.81	150.27
March	90.25	86.88	153.3	165.9	9.75	9.62	143.78	150.58

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FINANCIAL MARKETS

	Monetary Base		M1		M2		Federal Funds		T-Bills (6 Mos.)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	283.3	283.3	783.5	785.5	3037.5	3042.3	8.30	8.30	7.50	7.50
November	285.0	285.0	783.6	786.7	3054.0	3059.9	8.35	8.35	7.76	7.76
December	285.0	284.8	787.5	790.3	3066.2	3073.0	8.76	8.76	8.24	8.24
January 1989	288.6	289.6	789.3	786.4	3075.3	3070.1	9.02	9.12	8.38	8.36
February	291.3	289.5*	791.2	789.0*	3084.7	3074.3*	9.15	9.26*	8.53	8.46*
March	294.0	291.6	793.1	793.4	3093.2	3092.6	9.24	9.37	8.62	8.57
April	295.2	293.9	800.2	799.4	3120.6	3115.9	9.27	9.35	8.65	8.53
May	296.1	296.0	809.5	806.0	3143.2	3141.6	9.23	9.42	8.63	8.62
June	297.0	297.3	818.0	810.1	3166.5	3160.5	9.25	9.68	8.55	8.81
July	298.9	298.9	816.5	812.4	3180.2	3176.3	9.68	9.78	8.76	8.86
August	300.7	300.5	817.6	815.9	3193.1	3192.2	9.79	9.89	8.93	8.80
September	302.5	302.1	818.9	819.6	3207.3	3211.4	9.84	9.85	9.02	8.92
October	304.1	303.6	823.2	822.8	3223.5	3227.5	10.13	10.03	9.15	9.07
November	305.3	305.3	826.8	826.8	3246.1	3246.9	10.23	10.20	9.18	9.11
December	306.5	306.6	830.4	829.4	3269.0	3263.1	10.36	10.34	9.20	9.20
January 1990	308.5	308.4	836.3	833.3	3291.5	3278.4	10.35	10.36	9.17	9.15
February	310.3	309.9	842.8	836.7	3306.8	3291.8	10.38	10.42	9.15	9.21
March	312.1	311.6	848.9	842.3	3320.7	3313.8	10.34	10.40	9.12	9.20

	Aaa (Seasoned)		Municipals (Bond Buyer)		(3 Month) Commercial Paper		90 Day CD's		Prime Rate	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	9.51	9.51	7.47	7.47	8.24	8.24	8.36	8.36	10.00	10.00
November	9.45	9.45	7.46	7.46	8.66	8.66	8.78	8.78	10.05	10.05
December	9.57	9.57	7.61	7.61	9.11	9.11	9.25	9.25	10.50	10.50
January 1989	9.58	9.62	7.43	7.35	9.05	9.04	9.15	9.20	10.50	10.50
February	9.50	9.65*	7.38	7.52*	9.20	9.30*	9.29	9.43*	10.50	10.83*
March	9.46	9.68	7.35	7.55	9.26	9.38	9.35	9.49	10.50	11.00
April	9.40	9.65	7.31	7.52	9.38	9.39	9.43	9.50	10.50	11.00
May	9.47	9.73	7.40	7.61	9.35	9.45	9.45	9.56	10.50	11.00
June	9.54	9.82	7.52	7.70	9.40	9.65	9.49	9.73	10.50	11.23
July	9.83	9.89	7.73	7.78	9.65	9.76	9.76	9.84	11.00	11.50
August	9.92	10.04	7.80	7.85	9.76	9.91	9.84	10.03	11.00	11.50
September	10.01	10.01	7.88	7.83	9.86	9.87	9.93	9.97	11.39	11.50
October	10.20	10.15	7.96	7.92	10.15	10.13	10.24	10.26	11.58	11.86
November	10.36	10.18	8.11	7.96	10.24	10.22	10.35	10.35	12.00	12.00
December	10.25	10.26	8.20	8.11	10.35	10.35	10.46	10.44	12.00	12.00
January 1990	10.25	10.25	8.12	8.07	10.33	10.33	10.44	10.45	12.00	12.00
February	10.22	10.22	8.05	8.05	10.36	10.40	10.47	10.51	12.00	12.00
March	10.17	10.17	8.01	8.01	10.38	10.37	10.49	10.46	12.00	12.00

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ECONOMIC FORECASTING CENTER

MONTHLY PROJECTIONS
February 1989

Dr. Donald Ratajczak, Director
For Release: March 29, 1989

WHAT IS THE CASE FOR STAGFLATION?

As expected, robust economic indicators in January gave way to exceptionally sluggish indicators during February. However, with the exception of a surge in farm income, which caused personal income to soar above forecasted values for the first quarter, most indicators were close to February projections consistent with first-quarter estimates. The exceptions are auto sales, which are struggling to reach 10 million units at the present time, and construction, which is still growing faster than originally anticipated even after winter returned. Indeed, the 11.4% dip in housing starts still did not bring starts to a level that was below the 1988 averages. Sluggish manufacturing orders are only weak in comparison to the December levels, which soared dramatically. In February, shipments of nondefense capital goods trailed orders by more than $3.5 billion. Obviously, no near-term collapse in capital spending should be anticipated.

One area of concern is the significant acceleration of business inventories. After more than a year of modest inventory accumulations, manufacturers are rapidly adding to their inventories early in the new year. Some of this reflects goods in process and will be converted to shipments of capital goods later in the spring. However, some inventories may now be accumulated in anticipation of higher price increases. If such speculative inventories are building, this would be an early sign of a pending economic contraction.

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Unfortunately, February's sluggishness did not restrain price increases. A statistical fluke led to a 1% surge in the PPI for finished goods. An unusually small sample of geographic areas provided prices for fruits and vegetables. These prices should reverse next month. Unfortunately, a slight drought fear is again developing in the Midwest as a result of difficulties with the winter wheat crop. While only hard winter wheat is in jeopardy, these drought concerns could lead to significant increases in commodity prices. Indeed, food prices probably will rebound aside from the fruit and vegetable area in March.

More significantly, the increase in inflation at the commodity level is beginning to entice higher prices at the retail level. There is no simple relationship between commodity prices and inflation as measured by the Consumer Price Index. The Producer Price Index does not include imported goods while the CPI does. With the dollar strengthening during the past year, imported goods excluding oil are acting as a restraint upon inflationary pressures.

Also, some consumer resistence to higher prices, especially in clothing and some processed foods, has led to a narrowing of some profit margins. However, our samples show that supermarket margins in general have widened since the first of this year. Of greater interest are the lags between changes in commodity prices and changes in their finished goods components. For example, the February CPI continues to evaluate petroleum product as if oil were $15 per barrel. The Producer Price Index is evaluating oil products with oil priced $17.50 per barrel. In fact, low oil inventories have led to a scurry for increased oil as non-OPEC producers restrain their production. As a result, oil currently is being traded at more than $20 per barrel. These especially high oil prices are expected to settle back to only slightly more than $19 per barrel in the United States for the remainder of this year. Nevertheless, oil product prices have not increased at the retail level because consumer demand has been seasonally weak. When the driving season emerges, beginning at Easter, gasoline prices should rise significantly. Indeed, prices will rise between now and the Fourth of July by nearly 15¢ per gallon.

Thus, lags from commodity prices to finished goods prices depend upon seasonal demand characteristics, the degree of processing and handling that is required, and the amount of competitive pressures that prevail at the retail level.

Some analysts have maintained that price warfare, as evidenced by the Sears strategy to reduce prices on their products, is responsible for the absence of retail price pressures. Such an analysis misinterprets what Sears is trying to do. By lowering their everyday prices, they are trying to reduce the need for deep inventory-adjustment sales. Previously, the higher Sears prices caused people who needed a hammer or a screwdriver to go to Walmart. They would only show up at Sears during sales days. With everyday low prices, Sears hopes to recapture some of those customers. However, fewer sales and less discounting during the sales will materialize. Otherwise, Sears would give away too much of its returns to consumers rather than to shareholders, which is not the intent.

Moreover, the Consumer Price Index is 52% services. Service inflation notoriously lags commodity inflation and is transmitted through higher wage costs. As inflationary perceptions rise, wage pressures will intensify and this will accelerate the service deflator. However, by the time commodity inflation has been arrested by Federal Reserve restraints, higher wage pressures and rising service inflation will continue to generate accelerating consumer price indices.

As a result of this delayed response, especially in the service sector, some economists have claimed that a new era of stagflation is surfacing. This could be the case, especially if the administration decides that maintaining growth is more important than restraining inflation. Of course, such an assumption would require that the administration gradually tolerate higher and higher inflation rates. At least one economist maintained that slow growth and somewhat higher inflation could persist indefinitely. However, stagflation usually occurs as a result of raising the tolerance level for inflation in order to preserve growth. Of course, the ultimate result of such a policy is to lead to dramatically higher interest rates, reduced United States competitiveness in the world and an ultimate credit crunch to eventually eliminate the inflationary risk anyway. During the period of stagflation, manufacturers discover that profit objectives can be reached by raising prices. (This is partially true because accelerating inflation leads to inventory profits.) Sometimes, diligent costcutting is reduced as these profit margin gains are captured. Therefore, productivity deteriorates during such a stagflation period as well.

Whether a new bout of stagflation is about to occur depends upon the White House. Will they, in fact, support the Federal Reserve in trying to restrain inflation before it passes through to wage gains and ultimately to the service components, or will they try to preserve their real growth targets irrespective of the inflationary risk? The latter policy will lead to stagflation and a lot of other serious problems further down the road.

Quarterly Profile of GNP

	1988-4	1989-1	1989-2	1989-3	1989-4	1990-1	1988 Annual	1989 Annual
Real:	2.4	5.1	2.1	2.6	2.4	1.0	3.9	3.1
Price:	5.3	4.6	4.7	4.5	4.7	5.5	3.5	4.8
Nominal:	7.8	9.8	6.9	7.2	7.2	6.7	7.5	8.0

Monthly Statistical Highlights

	February 1989	March 1989	April 1989
Payroll Employment		+221,000	+206,000
Index of Hours Worked		+0.2%	+0.2%
Household Employment		+264,000	+214,000
Civilian Unemployment Rate		5.2%	5.2%
Personal Income		-0.1%	+0.6%
Savings Rate		5.3%	5.4%
Personal Consumption		+0.4%	+0.5%
Retail Sales		+0.4%	+1.5%
Auto Sales		9.8*	10.3*
Housing Starts		-1.5%	-4.1%
Housing Permits		+0.5%	-3.3%
Construction Expenditures	-1.5%	-0.6%	-2.0%
Business Inventories	+0.7%	+0.6%	+0.7%
Orders for Durable Goods		+2.4%	-1.7%
Orders for Nondefense Capital Goods		+6.7%	-3.7%
Industrial Production		+0.4%	+0.4%
CPI		+0.5%	+0.5%
PPI		+0.4%	+0.4%
Consumption Deflator		+0.4%	+0.4%
Leading Indicators	-0.3%	+0.2%	-1.6%
Currency Index		+1.8%	+1.7%
Equity Index		-2.9%	-0.1%
Real GNP (annual rate)	UNC	+2.7%	+1.8%
M1 (annual rate)		+2.9%	+2.9%
M2 (annual rate)		+3.8%	+4.9%

* auto sales in millions

Commentary

Employment - February's dip in the unemployment rate was concentrated in teenagers and young adults. Excluding that group, the unemployment rate showed little change. This suggests that statistical factors probably led to the decline in unemployment and some increases should be anticipated in the next few months. A decline in the index of hours worked was in the range anticipated a month ago as the workweek remained unchanged and employment grew. Employment gains of 60,000 in the government sector probably will not be repeated next month, but some rebound in manufacturing should be expected from sluggish February rates. The hourly earnings index increased only marginally, but the wage component of personal income showed sharp gains, suggesting that composition shifts rather than any wage restraint may have been responsible for the favorable hourly earnings report.

Increases in initial unemployment claims early in March suggest that economic activity remains sluggish. However, the insured unemployment rate remains unchanged, indicating that no significant long-term unemployment problems are yet developing.

Personal Income and Outlays - Personal income grew exceptionally strong in January and February as a result of a sharp rebound in farm income from $15 billion in December to $62 billion by February. On balance, farm income should average about $50 billion per month during the year. Thus, some retrenchment from the February farm numbers is anticipated. In addition, interest income is beginning to grow rapidly, increasing about 1.5% per month. As long as interest rates continue rising, rapid gains are expected in the interest component. Because of the growth in interest and temporary farm income, the surge in savings is not surprising and should not be viewed as a dramatic shift in consumer behavior. However, the consumer probably is seeking higher savings during these uncertain times.

All of the consumption growth in February was in the services sector, where a return to more normal weather led to a surge in utility purchases. There were also significant composition shifts in the services sector in February which led to minimal growth in the services deflator. These composition shifts will hold down the GNP deflator during the first quarter. Aside from the surge in services, other spending was weak. However, price increases should significantly accelerate nominal spending on nondurables in the next few months. The weakness in automobiles is harder to explain. Auto incentives have now been reinstituted and should accelerate sales late in March and in April.

Construction - Because of the mild weather, construction will be stronger during the first quarter than originally anticipated. Indeed, construction will actually contribute to GNP growth during the quarter. Weakness should develop as the spring develops, however. Little growth from current levels is expected in nonresidential expenditures. Exceptionally large increases in hotel and motel projects and commercial building during January probably will not be repeated. Housing probably will dip sharply. Although starts did not fall as much as anticipated, permits fell more than expected. Much of the permit weakness was in single-family units, which may not average more than 1 million during the year. With multi-families averaging slightly over 400,000, this suggests that housing starts will probably reach only 1.41 million for the year. This dip in housing will significantly slow construction spending programs during the summer months.

Construction materials continued to show minimal inflationary pressures as a result of apparent sluggishness in the sector. Also, labor costs remain well behaved. Some acceleration in labor costs are expected later in the year. Nevertheless, construction will probably be a restraining factor upon inflationary pressures in 1989 and prevent the GNP deflator from growing at the same rates as the consumer and producer price indices.

Business Activity - In their haste to announce sluggishness in the durable goods reports, which showed the first back-to-back declines in more than two years, many analysts failed to recognize that durable activity was at exceptionally high levels in December. Indeed, the slip in orders in February still places orders above anticipations of two months ago. Moreover, orders for nondefense capital goods are especially robust. In addition, commercial aircraft orders by American Airlines were not included in the monthly report. Therefore, a spurt in orders for nondefense capital goods could be expected next month. Orders for defense goods are near shipments at the present time and probably will show little movement in the next few months.

Some of the weakness in orders was the result of exceptionally strong backlogs developing in areas such as primary metals and transportation equipment. Because of delivery delays, orders are slowing. Once these delays diminish, orders will surge again.

Weakness in industrial production was slightly greater than anticipated as a result of a surprising 0.4% decline in production of industrial materials. Auto assemblies continued at 7.2 million, which is consistent with current projections of domestic auto sales for the year. Weakness in industrial materials is especially surprising as inventories have been increasing rapidly and as material prices have also been advancing. A reversal of this sluggish production in the materials sector is anticipated next month.

Prices - Auto incentives currently are restraining inflationary pressures at the consumer level. When those incentives are fully in place, some acceleration of consumer prices should be anticipated. CPI estimates for the year have been raised to 5.5% as measured on a December-to-December basis. PPI projections are approaching 6.0%. These are 1 and 2 percentage points respectively greater than their performance last year. Part of the acceleration is higher oil prices than originally anticipated. Not anticipating production reductions by non-OPEC producers, oil prices had been expected to fall in the spring. Unfortunately, that assumption proved to be in error. Oil prices now will probably average $4 more than originally projected.

Miscellaneous - Higher oil prices are going to restrain improvements in the merchandise trade balances over the next several months. Initially, foreign exchange traders will concentrate more upon interest rates than upon failure to improve trade balances. However, before the end of spring, the dollar is expected to come under renewed downward pressure. Nevertheless, high interest rates in the United States probably will prevent any dramatic selloff in the dollar this year.

Adjusted profits led to higher estimates of profits early in 1989 than originally anticipated. However, the rise in interest payments will prevent profits from rising during the year. In addition, a spurt in the inventory valuation adjustment will raise the tax liability of the corporate sector. Higher interest rates and a reduction in adjusted profits should lead to a significant decline in stock market values. A decline of 15% from current levels is anticipated before a stock market bottom is reached near the end of this year. This could lead the Dow Jones to fall to as low as 1900.

Financial Markets

Household savings grew sharply as farm income and interest income expanded. However, this increase in household savings has had little impact upon interest rate presures. As the houehold is not expected to significantly improve savings capabilities over the next year, this suggests that no further positive contribution upon credit market pressures will come from the household sector. Of course, higher interest rates will reduce housing demand. Therefore, net household use of funds may decline slightly, releasing some funds later in the year. At the present time, it appears that the household sector will have a marginal restraining effect upon interest rates for the remainder of this year after its significant shift in savings behavior has had little impact upon restraining interest rates early in the year.

The government sector probably already has reached its low point on deficits for the year. Government borrowing should intensify in the spring and early summer months. This, in turn, should exert upward pressures upon interest rates. In addition, the federal savings and loan bailout will replace short-term liabilities with long-term liabilities. This should lead to higher long-term interest rates. Thus, the yield curve will become less inverted, but partially because long-term interest rates will be under upward pressures.

As corporations build inventories and increase capital spending, their uses of funds will intensify. Apparently, their inventory rebuilding during the first quarter was more than enough to absorb household savings activity. Further strong corporate borrowings are anticipated as profitability gradually wanes during the spring and summer months. This would suggest that interest rates will continue to rise through the summer. Then, corporate activity may gradually become restrained, eventually leading to declining interest rates by year's end.

Of course, the foreign investor will be a dominant player in interest rate movements. At this time, foreign capital is moving into the United States as interest rates are rising here and economic activity appears robust. If a recession looms, however, foreign investors probably would try to withdraw funds. This could preserve high interest rates into 1990.

Equity Markets - As mentioned above, adjusted profitability should quickly erode as inventory profits raise tax liabilities and interest burdens reduce the favorable cash flow of corporations. This should be apparent by the second quarter. In addition, rising interest rates will lower the value of any earnings potential. For these reasons, the stock market probably will be heading downward very shortly. A decline of 15% currently is anticipated.

Although some purchases of defensive stocks, such as consumer-oriented issues, could prove valuable, it probably is too early to purchase interest-sensitive issues. For that reason, some liquidation in equity positions would be recommended at the present time.

EMPLOYMENT

	Payroll Employment		Index of Hours Worked		Household Civilian Employment		Civilian Unemployment Rate		Hourly Earnings	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	106973	106973	127.1	127.1	115573	115573	5.3	5.3	9.43	9.43
November	107377	107419	127.0	127.1	115947	115947	5.4	5.4	9.42	9.42
December	107656	107641	127.1	127.2	116009	116009	5.3	5.3	9.44	9.45
January 1989	108026	108056	127.6	128.3	116435	116711	5.3	5.4	9.50	9.50
February	108277	108345	128.0	127.9	116700	116853	5.2	5.1	9.55	9.51
March	108526	108566*	128.4	128.1*	116965	117117*	5.2	5.2*	9.60	9.56*
April	108753	108772	128.7	128.4	117168	117331	5.1	5.2	9.63	9.60
May	108960	108994	129.0	128.6	117381	117583	5.0	5.1	9.66	9.64
June	109165	109216	129.2	128.8	117592	117827	5.0	5.1	9.68	9.68
July	109328	109427	129.4	129.0	117746	118051	5.0	5.0	9.72	9.71
August	109555	109633	129.7	129.3	117980	118277	5.0	5.0	9.77	9.75
September	109784	109821	129.9	129.5	118221	118495	4.9	5.0	9.81	9.79
October	109938	110052	130.0	129.7	118403	118733	4.9	4.9	9.85	9.84
November	110037	110228	130.2	129.9	118559	118922	4.9	4.9	9.90	9.88
December	110235	110423	130.3	130.1	118716	119077	4.9	5.0	9.95	9.93
January 1990	110423	110586	130.6	130.3	118914	119253	4.8	5.0	9.99	9.97
February	110617	110694	130.8	130.4	119151	119391	4.8	5.1	10.04	10.02
March	110809	110729	131.1	130.4	119362	119440	4.9	5.2	10.09	10.07

PERSONAL INCOME

	Personal Income		Wage & Salary		Personal Savings		Disposable Income		Personal Outlays	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	4.184	4.178	2.512	2.508	182.9	174.0	3.587	3.583	3.404	3.409
November	4.175	4.170	2.520	2.516	153.3	150.1	3.577	3.573	3.423	3.423
December	4.196	4.201	2.522	2.530	157.6	150.4	3.598	3.600	3.440	3.449
January 1989	4.223	4.273	2.543	2.550	167.9	198.3	3.620	3.660	3.452	3.462
February	4.272	4.315	2.571	2.573	189.6	219.6	3.664	3.700	3.474	3.480
March	4.320	4.309*	2.599	2.593*	206.3	196.3*	3.702	3.692*	3.496	3.496*
April	4.343	4.336	2.608	2.611	200.6	201.4	3.719	3.716	3.518	3.515
May	4.366	4.362	2.617	2.628	196.7	203.6	3.734	3.739	3.537	3.535
June	4.389	4.388	2.626	2.644	197.3	205.9	3.750	3.761	3.553	3.555
July	4.412	4.410	2.645	2.658	197.1	214.0	3.773	3.778	3.576	3.564
August	4.434	4.437	2.665	2.677	199.8	207.8	3.797	3.801	3.597	3.593
September	4.456	4.459	2.686	2.692	201.8	205.3	3.820	3.818	3.618	3.613
October	4.479	4.485	2.699	2.711	195.3	210.8	3.835	3.840	3.640	3.629
November	4.501	4.508	2.712	2.728	192.7	199.4	3.852	3.859	3.659	3.660
December	4.523	4.532	2.725	2.747	191.1	198.1	3.868	3.879	3.677	3.681
January 1990	4.552	4.550	2.744	2.764	194.2	191.1	3.895	3.893	3.701	3.702
February	4.582	4.577	2.764	2.781	202.5	203.7	3.926	3.917	3.724	3.713
March	4.613	4.602	2.785	2.797	209.4	196.7	3.953	3.938	3.744	3.741

Fore. = February Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

CONSUMPTION

	Personal Consumption Fore.	Personal Consumption C.E.	Durables Fore.	Durables C.E.	Nondurables Fore.	Nondurables C.E.	Services Fore.	Services C.E.	Consumption Real Fore.	Consumption Real C.E.
October 1988	3302.9	3307.0	452.0	453.3	1071.3	1071.3	1778.8	1782.4	2613.6	2616.9
November	3321.6	3320.3	453.6	458.7	1077.4	1080.9	1782.6	1780.7	2617.9	2623.5
December	3335.8	3346.0	472.1	480.2	1076.9	1069.4	1795.5	1796.4	2635.4	2634.6
January 1989	3349.1	3357.9	460.7	461.1	1080.5	1088.1	1807.6	1808.6	2628.8	2627.2
February	3371.0	3375.7	463.5	459.7	1085.6	1089.0*	1821.9	1827.0*	2637.7	2636.6
March	3391.9	3390.8*	466.5	463.2*	1090.8	1093.9	1834.6	1833.7	2643.7	2638.9*
April	3414.1	3409.1	470.2	469.5	1097.4	1100.1	1846.5	1839.5	2646.6	2642.1
May	3432.5	3429.3	472.4	470.8	1101.3	1112.3	1858.5	1846.2	2648.5	2648.4
June	3447.4	3448.4	471.6	471.9	1105.5	1119.6	1870.3	1856.9	2647.8	2652.1
July	3470.1	3456.6	474.3	465.8	1113.4	1122.5	1882.4	1868.3	2655.0	2645.6
August	3490.9	3485.1	476.8	475.6	1118.6	1129.1	1895.5	1880.4	2662.8	2658.2
September	3511.4	3503.9	479.3	476.7	1123.9	1134.7	1908.2	1892.5	2670.3	2663.3
October	3532.3	3519.7	481.5	475.6	1130.1	1138.8	1920.7	1905.3	2671.9	2664.9
November	3551.1	3549.4	483.3	485.7	1134.0	1145.9	1933.8	1917.8	2672.0	2676.1
December	3567.9	3569.9	483.3	488.9	1138.0	1151.1	1946.6	1929.9	2672.6	2678.7
January 1990	3591.6	3590.1	486.5	491.4	1146.2	1157.1	1958.9	1941.6	2680.3	2681.8
February	3614.0	3600.8	489.4	485.0	1151.9	1161.3	1972.7	1954.5	2687.0	2676.9
March	3633.8	3628.2	490.2	492.0	1157.5	1168.8	1986.3	1967.4	2691.7	2687.3

RETAIL SALES

	Retail Sales Fore.	Retail Sales C.E.	Non-Auto Durables Fore.	Non-Auto Durables C.E.	Auto (Million Units) Fore.	Auto (Million Units) C.E.	Nondurable Sales Fore.	Nondurable Sales C.E.	Auto Sales Fore.	Auto Sales C.E.
October 1988	136.56	136.56	20.90	20.90	9.8	9.9	85.36	85.36	30.30	30.30
November	137.81	137.87	21.10	21.10	10.2	10.2	85.80	85.80	30.91	30.91
December	138.03	137.86	21.51	21.79	11.7	11.6	85.70	85.24	30.82	30.83
January 1989	138.04	138.85	21.27	22.15	9.9	9.8	86.04	86.41	30.73	30.30
February	138.77	138.23	21.16	21.97	10.3	9.9	86.45	86.48	31.16	29.79
March	139.52	138.73*	21.13	22.14*	10.7	9.8*	86.86	86.83*	31.53	29.76*
April	140.47	140.86	21.58	22.26	10.6	10.3	87.39	87.32	31.50	31.28
May	141.03	141.57	21.57	22.15	10.7	10.4	87.70	87.89	31.76	31.53
June	141.27	142.27	21.65	22.49	10.6	10.3	88.03	88.46	31.59	31.32
July	141.50	142.21	21.88	22.67	10.2	10.1	88.66	88.69	30.96	30.85
August	142.90	143.44	22.24	22.74	10.5	10.5	89.08	89.21	31.58	31.49
September	143.60	144.02	21.99	22.70	10.8	10.7	89.50	89.66	32.11	31.66
October	144.34	143.76	22.38	22.85	10.1	9.8	89.99	89.98	31.97	30.93
November	144.86	145.46	22.23	23.06	10.3	10.2	90.30	90.54	32.33	31.86
December	145.18	146.23	21.80	22.99	10.6	10.4	90.62	90.95	32.76	32.29
January 1990	146.19	147.00	22.33	23.11	10.5	10.5	91.27	91.43	32.59	32.46
February	146.97	146.60	22.56	23.10	10.6	10.2	91.73	91.76	32.68	31.74
March	147.49	147.98	22.70	22.95	10.5	10.5	92.17	92.35	32.62	32.68

Fore. = February Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

CONSTRUCTION

	Housing Starts		Single Family Starts		Housing Permits		Construction Expenditures (Current)		Construction Expenditures (Real)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	1.542	1.532	1.112	1.136	1.516	1.516	407.8	408.2	349.8	350.1
November	1.563	1.567	1.151	1.138	1.517	1.516	411.1	413.6	352.6	354.7
December	1.506	1.577	1.121	1.141	1.502	1.566	408.2	422.3	349.2	361.4
January 1989	1.490	1.690	1.095	1.202	1.473	1.507	410.3	424.0	350.4	363.8
February	1.443	1.498	1.063	1.045	1.416	1.404	409.8	417.5*	349.7	357.4*
March	1.405	1.476*	1.032	1.026*	1.372	1.411*	409.4	414.9	348.7	354.9
April	1.457	1.416	1.056	1.003	1.375	1.365	409.3	406.8	348.0	347.4
May	1.490	1.384	1.084	0.976	1.413	1.328	409.5	404.2	347.3	344.6
June	1.466	1.380	1.055	0.971	1.392	1.336	409.3	401.2	346.6	341.2
July	1.438	1.389	1.037	0.978	1.375	1.321	411.9	401.5	347.9	340.8
August	1.414	1.366	1.025	0.955	1.356	1.296	413.2	402.3	347.8	340.9
September	1.423	1.387	1.011	0.972	1.364	1.299	414.4	405.1	347.7	342.4
October	1.425	1.402	1.020	0.983	1.343	1.315	414.3	407.1	346.7	343.5
November	1.413	1.392	1.012	0.991	1.327	1.311	414.6	409.3	346.1	344.5
December	1.414	1.400	1.018	1.003	1.330	1.318	414.5	411.4	344.8	345.4
January 1990	1.369	1.426	0.984	1.005	1.306	1.321	414.9	414.5	344.0	347.2
February	1.358	1.430	0.976	1.009	1.298	1.316	416.1	417.0	343.9	348.1
March	1.345	1.425	0.968	1.013	1.299	1.315	417.4	418.7	343.5	348.3

	Non-Residential		Public Construction		Residential Construction	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	130.9	130.7	77.9	77.9	199.0	199.6
November	129.7	131.5	80.9	80.3	200.4	201.8
December	128.4	134.1	79.5	85.9	200.3	202.3
January 1989	128.8	137.7	81.0	81.7	200.5	204.6
February	128.4	133.6*	80.6	80.8*	200.8	203.1*
March	127.8	133.5	81.5	81.3	200.1	200.1
April	128.3	134.0	81.7	81.6	199.3	191.2
May	128.8	133.7	82.0	82.4	198.7	188.1
June	129.2	133.3	82.0	82.1	198.1	185.8
July	129.5	133.1	82.5	82.5	199.9	185.9
August	129.8	132.5	82.6	82.9	200.8	186.9
September	130.1	132.7	82.8	83.3	201.5	189.1
October	130.4	133.1	83.0	83.5	200.9	190.5
November	130.6	133.0	83.2	83.6	200.8	192.7
December	130.9	133.4	82.8	83.3	200.8	194.7
January 1990	131.5	133.4	83.5	84.2	199.9	196.9
February	132.3	133.7	84.2	84.5	199.6	198.8
March	133.1	133.9	84.9	85.1	199.4	199.7

Fore. = February Forecast
C.E. = Current Expectations
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BUSINESS ACTIVITY

	Manufacturers' Inventories		Durable Goods Orders		Non-Defense Capital Goods Orders		Non-Defense Capital Shipments	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	349.4	349.4	122.79	122.79	34.62	34.62	32.69	32.60
November	350.9	351.6	122.77	123.04	35.67	35.83	32.43	32.51
December	352.4	354.2	121.85	132.15	34.23	39.43	32.47	32.68
January 1989	354.3	357.3	123.74	128.28	34.93	40.31	32.96	33.31
February	356.8	360.5*	122.19	123.68	33.67	36.73	33.02	33.16
March	359.2	363.4	122.85	126.65*	33.84	39.19*	33.10	33.46*
April	361.5	366.1	123.75	124.48	34.26	37.74	33.43	33.69
May	363.6	368.5	123.14	124.16	34.05	37.05	33.88	34.03
June	365.8	370.3	123.67	122.91	34.35	35.63	34.25	34.09
July	367.9	372.5	124.51	123.37	34.97	35.54	34.56	34.65
August	369.5	374.9	125.89	124.72	35.37	36.19	34.65	34.88
September	372.3	376.3	125.11	124.56	35.11	36.28	34.47	35.21
October	374.6	378.4	124.48	123.28	34.96	35.84	34.69	35.56
November	376.8	380.1	125.93	125.16	35.22	36.26	34.83	35.92
December	378.9	382.4	126.21	124.86	35.29	36.04	34.98	36.16
January 1990	381.1	384.3	127.72	124.43	35.56	35.73	35.15	36.24
February	382.4	386.5	127.85	124.21	36.42	35.65	35.70	36.15
March	383.7	388.7	127.56	124.16	36.40	35.49	36.28	36.09

	Business Inventories		Defense Shipments		Industrial Production		Capacity Utilization	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	751.4	750.6	8.43	8.43	139.3	139.4	84.0	84.0
November	754.4	753.7	8.55	8.66	139.9	139.9	84.2	84.1
December	755.0	760.6	8.63	10.10	140.2	140.5	84.1	84.3
January 1989	760.6	766.2	8.54	8.69	140.8	141.1	84.3	84.5
February	766.5	771.4*	8.51	8.22	141.2	141.1	84.4	84.3
March	772.3	776.3	8.43	8.43*	141.6	141.6*	84.5	84.5*
April	775.7	781.9	8.50	8.37	142.3	142.1	84.8	84.6
May	779.6	786.9	8.55	8.44	142.7	142.5	84.9	84.7
June	783.4	790.6	8.56	8.56	143.2	143.0	85.1	84.8
July	788.1	795.1	8.53	8.52	143.4	143.4	85.0	84.8
August	792.0	800.4	8.55	8.93	143.2	143.9	84.7	85.0
September	795.8	805.6	8.56	9.14	143.5	144.3	84.7	85.1
October	801.1	810.3	8.59	8.72	143.7	144.7	84.6	85.1
November	806.6	815.9	8.61	8.59	143.8	145.0	84.5	85.1
December	812.1	820.4	8.63	8.67	143.9	145.2	84.4	85.0
January 1990	815.3	824.3	8.60	8.69	144.1	145.4	84.3	85.0
February	818.2	828.8	8.65	8.58	144.3	145.3	84.2	84.7
March	821.1	832.4	8.73	8.68	144.6	145.1	84.2	84.3

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PRICES

	CPI-U (seasonally adjusted)		PPI Finished Goods (seasonally adjusted)		PPI-Industrial Commodities (unadjusted)		Estimated GNP Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	119.9	119.9	109.5	109.5	107.1	107.1	123.4	123.5
November	120.3	120.3	109.8	109.8	107.4	107.4	123.8	124.0
December	120.8	120.7	110.3	110.2	108.1	108.1	124.2	124.4
January 1989	121.2	121.3	110.8	111.3	108.7	109.1	124.5	124.8
February	121.5	121.8	111.1	112.4	109.0	109.6	124.8	125.2
March	121.8	122.4*	111.4	112.8*	109.1	110.1*	125.1	125.7
April	122.4	122.9	111.8	113.3	109.7	110.8	125.6	126.2
May	122.9	123.4	112.1	113.7	110.2	111.3	126.1	126.6
June	123.3	123.9	112.4	114.1	110.6	111.8	126.5	127.1
July	124.0	124.6	112.8	114.6	111.3	112.5	127.0	127.6
August	124.7	125.1	113.3	115.0	111.8	113.0	127.4	128.0
September	125.4	125.6	113.9	115.5	110.5	111.7	127.8	128.4
October	125.9	126.1	114.4	116.0	111.8	113.3	128.4	128.8
November	126.3	126.6	114.8	116.4	112.1	113.7	128.9	129.3
December	126.7	127.3	115.1	116.9	112.4	114.1	129.5	129.9
January 1990	127.3	127.9	115.6	117.4	113.0	114.7	129.9	130.5
February	127.9	128.5	116.3	117.8	113.6	115.4	130.3	131.1
March	128.5	129.0	117.0	118.2	114.1	116.0	130.7	131.6

	Consumption Deflator		Consumer Durables		Consumer Nondurables		Consumer Services		Implicit Construction Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	126.4	126.4	111.0	111.1	118.4	118.4	136.8	136.8	116.6	116.6
November	126.6	126.6	111.1	111.1	118.2	118.2	137.3	137.3	116.6	116.6
December	126.9	127.0	111.8	112.0	118.4	118.4	137.8	137.9	116.9	116.9
January 1989	127.4	127.8	112.0	111.8	118.6	119.2	138.4	138.9	117.1	116.6
February	127.8	128.0	112.3	111.7	118.7	119.5	138.9	139.1	117.2	116.8*
March	128.3	128.5*	112.6	111.9*	119.4	119.9*	139.3	139.7*	117.4	116.9
April	129.0	129.0	112.9	112.3	120.2	120.5	140.0	140.3	117.6	117.1
May	129.6	129.5	113.1	112.6	120.9	120.9	140.8	140.9	117.9	117.3
June	130.2	130.0	113.3	113.0	121.5	121.4	141.5	141.5	118.1	117.6
July	130.7	130.7	113.7	113.3	121.8	121.8	142.1	142.3	118.4	117.8
August	131.1	131.1	114.1	113.7	122.0	122.2	142.7	142.9	118.8	118.0
September	131.5	131.6	114.5	114.0	122.3	122.5	143.3	143.5	119.2	118.3
October	132.2	132.1	114.8	114.3	123.0	122.9	144.0	144.1	119.5	118.5
November	132.9	132.6	115.1	114.6	123.8	123.5	144.7	144.8	119.8	118.8
December	133.5	133.3	115.4	114.9	124.6	124.2	145.4	145.5	120.2	119.1
January 1990	134.0	133.9	115.7	115.2	124.9	124.8	146.0	146.2	120.6	119.4
February	134.5	134.5	116.0	115.6	125.1	125.3	146.7	146.9	121.0	119.8
March	135.0	135.0	116.3	115.9	125.4	125.7	147.4	147.6	121.5	120.2

Fore. = February Forecast
C.E. = Current Expectations
* _ = This item and those beyond it are projections.

MISCELLANEOUS

	Merchandise Trade Balance		Leading Indicators	Estimated GNP		Estimated GNP (1982 $)		IVA (annual rate)	
	Fore.	C.E.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	-8.88	-8.88	143.9	4963	4970	4022	4024	-24.4	-20.6
November	-10.18	-10.38	143.9	4984	5001	4026	4033	-20.7	-18.7
December	-9.96	-10.92	144.9	5023	5033	4044	4046	-20.6	-18.3
January 1989	-10.26	-9.49*	145.7	5066	5092	4069	4080	-20.1	-20.5
February	-10.72	-10.19	145.2*	5085	5108	4075	4080	-21.4	-24.6
March	-10.35	-10.36	145.5	5120	5140	4093	4089	-22.7	-27.3
April	-10.11	-9.48	143.2	5153	5168	4103	4095	-21.9	-30.5
May	-10.01	-9.76	142.6	5186	5193	4113	4107	-21.5	-28.6
June	-9.86	-9.89	144.2	5219	5230	4126	4115	-21.3	-27.2
July	-9.95	-9.53	143.7	5237	5264	4124	4125	-25.9	-25.3
August	-9.81	-9.26	144.1	5258	5289	4127	4132	-28.3	-23.8
September	-9.65	-10.13	144.5	5279	5316	4131	4140	-31.0	-24.9
October	-9.55	-10.05	144.1	5305	5350	4132	4154	-27.6	-26.2
November	-9.94	-9.73	142.8	5334	5375	4138	4157	-25.3	-25.3
December	-10.28	-9.52	140.9	5362	5403	4141	4159	-23.1	-21.8
January 1990	-9.79	-9.26	140.7	5390	5439	4149	4168	-29.6	-24.4
February	-9.71	-8.95	140.9	5417	5462	4157	4166	-31.3	-26.7
March	-9.64	-8.99	141.2	5445	5484	4166	4167	-33.0	-26.1

	Currency Index		Adjusted Profits		30-Year Government Bonds		New York Composite	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	95.10	95.10	185.4	190.5	8.89	8.89	156.36	156.36
November	91.91	91.91	186.9	189.6	9.02	9.02	152.67	152.67
December	92.65	91.88	177.3	202.8	9.01	9.01	155.34	155.35
January 1989	95.43	95.12	182.2	211.3	8.92	8.93	158.53	160.40
February	97.22	95.53	181.1	207.6	9.03	9.01	161.46	165.08
March	96.25	97.23*	179.9	204.3	9.04	9.23	161.06	160.32*
April	94.43	98.84	178.5	205.7	8.86	9.30	163.49	160.20
May	93.36	98.53	177.2	201.6	8.73	9.46	162.25	154.36
June	92.71	96.47	175.8	198.4	9.02	9.59	158.07	149.85
July	92.43	95.51	171.2	193.6	9.38	9.53	154.62	147.14
August	92.00	93.27	169.3	195.2	9.53	9.68	151.72	146.06
September	91.66	94.42	167.6	188.4	9.51	9.72	148.85	140.39
October	90.43	94.81	166.8	183.5	9.63	9.51	150.25	139.76
November	86.55	95.16	165.5	180.9	9.69	9.60	149.53	136.49
December	86.92	94.71	164.5	181.2	9.83	9.43	148.86	139.18
January 1990	90.43	92.21	160.2	180.5	9.80	9.21	145.79	141.95
February	91.67	92.16	156.5	179.6	9.79	9.17	144.81	141.86
March	90.25	91.43	153.3	180.3	9.75	9.04	143.78	144.46

Fore. = February Forecast
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* = This item and those beyond it are projections.

FINANCIAL MARKETS

	Monetary Base		M1		M2		Federal Funds		T-Bills (6 Mos.)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	283.3	283.8	783.5	785.4	3037.5	3042.2	8.30	8.30	7.50	7.50
November	285.0	284.6	783.6	786.6	3054.0	3059.1	8.35	8.35	7.76	7.76
December	285.0	285.0	787.5	790.2	3066.2	3071.8	8.76	8.76	8.24	8.24
January 1989	288.6	288.0	789.3	786.3	3075.3	3069.0	9.02	9.12	8.38	8.36
February	291.3	287.4*	791.2	787.4	3084.7	3070.3	9.15	9.36	8.53	8.55
March	294.0	288.0	793.1	789.3*	3093.2	3079.8*	9.24	9.83*	8.62	8.86*
April	295.2	289.3	800.2	791.2	3120.6	3092.2	9.27	10.06	8.65	9.11
May	296.1	290.5	809.5	793.1	3143.2	3103.6	9.23	10.02	8.63	9.07
June	297.0	292.4	818.0	797.4	3166.5	3120.4	9.25	10.27	8.55	9.20
July	298.9	293.5	816.5	801.3	3180.2	3135.7	9.68	10.35	8.76	9.29
August	300.7	294.6	817.6	804.8	3193.1	3154.5	9.79	10.56	8.93	9.43
September	302.5	295.5	818.9	808.2	3207.3	3173.4	9.84	10.84	9.02	9.65
October	304.1	296.8	823.2	811.7	3223.5	3192.4	10.13	10.83	9.15	9.63
November	305.3	298.0	826.8	815.9	3246.1	3208.9	10.23	10.59	9.18	9.28
December	306.5	300.3	830.4	820.8	3269.0	3228.2	10.36	10.46	9.20	9.15
January 1990	308.5	301.6	836.3	823.7	3291.5	3244.3	10.35	10.45	9.17	9.07
February	310.3	303.2	842.8	826.8	3306.8	3260.5	10.38	10.29	9.15	8.93
March	312.1	305.1	848.9	830.9	3320.7	3276.7	10.34	10.27	9.12	8.95

	Aaa (Seasoned)		Municipals (Bond Buyer)		(3 Month) Commercial Paper		90 Day CD's		Prime Rate	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	9.51	9.51	7.47	7.47	8.24	8.24	8.36	8.36	10.00	10.00
November	9.45	9.45	7.46	7.46	8.66	8.66	8.78	8.78	10.05	10.05
December	9.57	9.57	7.61	7.61	9.11	9.11	9.25	9.25	10.50	10.50
January 1989	9.58	9.62	7.43	7.35	9.05	9.04	9.15	9.20	10.50	10.50
February	9.50	9.64	7.38	7.44	9.20	9.37	9.29	9.51	10.50	10.93
March	9.46	9.87*	7.35	7.69*	9.26	9.89*	9.35	10.13*	10.50	11.48*
April	9.40	10.02	7.31	7.83	9.38	10.13	9.43	10.32	10.50	11.76
May	9.47	10.20	7.40	7.94	9.35	10.08	9.45	10.30	10.50	12.00
June	9.54	10.36	7.52	8.02	9.40	10.29	9.49	10.46	10.50	12.00
July	9.83	10.30	7.73	7.93	9.65	10.36	9.76	10.51	11.00	12.00
August	9.92	10.45	7.80	8.11	9.76	10.45	9.84	10.60	11.00	12.13
September	10.01	10.52	7.88	8.21	9.86	10.76	9.93	10.89	11.39	12.50
October	10.20	10.32	7.96	8.07	10.15	10.70	10.24	10.84	11.58	12.50
November	10.36	10.39	8.11	8.14	10.24	10.52	10.35	10.65	12.00	12.50
December	10.25	10.22	8.20	8.03	10.35	10.37	10.46	10.49	12.00	12.50
January 1990	10.25	10.05	8.12	7.92	10.33	10.33	10.44	10.45	12.00	12.36
February	10.22	10.01	8.05	7.87	10.36	10.26	10.47	10.37	12.00	12.00
March	10.17	9.92	8.01	7.78	10.38	10.21	10.49	10.32	12.00	12.00

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ECONOMIC FORECASTING CENTER

MONTHLY PROJECTIONS
March 1989

Dr. Donald Ratajczak, Director
For Release: April 24, 1989

HAS THE INFLATION WAR BEEN WON?

Following the slowdown to 0.4% in the PPI for March and the 0.5% increase in the CPI for the same month, some Wall Street analysts have already declared that the inflation war has been won by the Federal Reserve. Is this a shrewd analysis of developing economic trends or is it an Aikenism. (During the Vietnam conflict, Senator Aiken from Vermont declared that we could solve the Vietnamese problem by merely declaring that we had won and then get out.)

Certainly, economic growth has slowed in recent months. February's slowing was the result of shifting seasonal patterns, but the persistence of economic slowing in March clearly indicates that high interest rates are beginning to slow several sectors of the economy. First, housing activity has slowed significantly, with March permits declining to a level consistent with only 1.3 million starts. Housing starts almost certainly will average less than 1.4 million this year. Second, high interest rates are beginning to shift the savings desires of consumers. Consumer durable spending other than for automobiles is slowing while automobile sales require incentives to maintain previous-year levels. Third, the restrictive monetary activity has led to a relatively strong dollar. This in turn has begun to slow export growth and encourage further import activity. Thus, trade balances appear to be stalled at more than $10 billion deficits per month.

These sources of reduced growth or absolute decline cannot be offset by modest inventory accumulations and continued significant growth in capital

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spending. Certainly, there is not enough government spending growth to offset this slowing. Therefore, economic growth probably will fall well below the 2.5% growth path dictated by the Federal Reserve by the second half of this year. As the Federal Reserve almost certainly will be able to accomplish its growth objectives during the latter half of this year, some analysts have assumed that monetary ease is now appropriate.

However, such a conclusion assumes that achieving the Federal Reserve target on economic growth will also achieve the Federal Reserve desires to slow inflationary pressures. Eventually, slow economic growth will lead to rising unemployment, slower wage growth, and slower inflation. However, initially, inflationary forces can continue to intensify. Thus, in order to achieve an objective of preventing inflation from exceeding 5% at annual rates, more stringent monetary activity is necessary. In short, the casualties to economic growth are growing but the victory over inflation is no where in sight.

Indeed, after adjustment for pecularities in the PPI index, the March figures do not really indicate a slowing of inflationary pressures in the commodity markets. When the surprising 1.0% increase in the January PPI was reported, it was noted that seasonal adjustment changes added 0.4 percentage points to this January's index relative to previous years. In March, the seasonals were expected to reduce price pressures by 0.2 percentage points. Indeed, at that time, we remarked that it would truly be surprising if inflationary pressures moved from a measured 12% annual rate in January to only a 2% annual rate by March.

Of course, a continuation of 1.0% gains in February seemed to imply that a ratcheting up of inflation actually occurred. Instead, measurement problems associated with fruits and vegetables may have added as much as 0.3 percentage points to the February finished goods index. In March, with both a reversal of the fruit and vegetable problems and an adjustment to the January excessive seasonal factors, the market should have been surprised if a dramatic slowing in the PPI did not occur. Unfortunately, until the oil price increases run their course, commodity inflation probably is in excess of 6% at annual rates. Thus, some acceleration of PPI increases almost certainly should occur during the next several months.

As for the slowing in the CPI, only the sharp price decline in house furnishings gave any inkling that economic slowing was leading to slower inflationary pressures. Of course, rising egg prices, that led to sharp price increases in the foods, should not persist. Also, clothing prices will not rise sharply after April. Indeed, if patterns of the past two years continue, clothing prices could decline in June and July. Also, new auto incentives should lower prices for automobiles and also for automobile financing during April. On the other hand, the March CPI was only consistent with $16 oil. With wet barrels of oil selling in excess of $23 following the Alaskan oil spill and the explosion in the Brent fields, a 20% increase in gasoline prices from March levels could develop. Surveys by AAA and Lundberg indicate that 15¢ of that increase may have developed in April alone. If so, the gasoline component of the CPI will contribute almost 0.5 percentage points to that month's index. Another 0.1 to 0.2 percentage points probably will surface in May. Thus, stronger consumer price increases are expected for several more months.

Of course, it is easy to declare that one-time oil price changes are generating these price increases. Thus, they are having little effect upon underlying inflation. When the oil price pressures ease later this year, inflation rates should move toward their basic trend path. Such an argument is partially valid, but the trend inflation rate is not totally independent of food and energy price changes. If strong food and energy price increases persist, purchasing power will erode just as if the price increases were in clothing, drugs, or other CPI components. Moreover, gasoline and food more readily add to inflationary fears than other price changes. Thus, the inflationary expectations that drive wage demands almost certainly will be altered by this first-half explosion of energy prices. This, in turn, will lead to accelerating hourly earnings and rising wage costs. By the time commodity inflation slows to less than 5% rates of increase later this year, hourly wage increases probably will be accelerating to more than 5%.

Moreover, the slow growth engineered by the Federal Reserve almost certainly will slow productivity performance. Thus, unit labor costs probably will also be growing in excess of 5%. Before year-end, service inflation could be moving toward 6% rates of gain.

Moreover, the unemployment rate will be slow to rise. As a result, other laborers will try to repeat the wage performances that currently are being achieved in the service economy. Union wages, which have actually aided the moderation of wage inflation should accelerate significantly as the copper and then steel industries negotiate in the late spring and early summer months. In short, if underlying inflation can be approximated by a four-quarter moving average of unit labor costs, that inflationary measure will not reach its peak until late this year or early in 1990. The only way to get a significant slowing in inflation before then is to actually reverse commodity inflation, causing it to fall later this year.

Certainly, a substantial economic correction could do just that. In addition, if the oil cartel falls apart, falling oil prices could greet us in the fall just as rising oil prices were catapulted by the spring. However, any movement toward monetary ease at the present time would not create such a collapse in commodity prices. Moreover, world oil demand is now rising faster than world growth, a condition that did not previously occur since 1972. A collapse in the oil cartel is not likely under such conditions.

Of more significance is the absence of any signs that commodity inflation is even slowing after excluding food and energy. Sensitive crude prices excluding food and energy accelerated by more than 2% in the March PPI report. The Journal of Commerce indicators, which include oil but also measure other industrial materials as well, have reached new highs in recent days. Even without the influence of oil, those sensitive prices would be rising.

Of course, the Wall Street analysts may be missing this continuing strength in commodity prices because they are looking at the CRB index. That index is heavily weighted by animal and grain prices. Slaughters have increased in the Midwest as a result of further drought fears. As a result, livestock prices temporarily are falling. At the same time, a significant increase in agricultural acreage is raising prospects that grain prices may not rise significantly this year. If so, basic foodstuff prices may stabilize. Eventually, this could lead to stability in meat prices and a return to the 3% to 5% price increases that grocery store prices have experienced until last year's drought. However, such food price relief is not likely to be significant until next year.

Thus, the war against inflation has not been won. Indeed, if the dollar plummets sharply when foreign investors discover that interest rates and monetary restraint no longer are expected to intensify here even as they are starting to rise abroad, greater inflation could develop. Those declaring that the war was won may cause a shift in policy that could assure that the war is lost.

Obviously, this reasoning suggests that financial markets have become too exuberant. Stock prices in particular appear to be especially vulnerable. They are assuming that inflation will slow without damaging revenues as much as restraining cost pressures. In reality, the price lags are just the reverse. For that reason, corporate profitability almost certainly is being grossly exaggerated on current analysts' sheets. When this becomes obvious, a stock market correction appears to be inevitable.

However, even a correction in the bond market could develop. While interest rates probably will decline in 1990 after the economic slowing finally leads to sufficient increases in unemployment to stall further wage growth, the initial response to increasing inflationary measures in April and May could be a sign of panic. Thus, the long bond could very well rise sharply by more than a half percentage point during the next few weeks. Certainly, anyone who remembers bond trading during the quarterly funding the previous several Mays should be quite happy to take profits under current conditions.

Quarterly Profile of GNP

	1988-4	1989-1	1989-2	1989-3	1989-4	1990-1	1988 Annual	1989 Annual
Real:	2.4	5.1	2.0	2.6	1.9	1.5	3.9	3.0
Price:	5.3	4.7	5.1	4.8	4.6	4.9	3.5	5.0
Nominal:	7.8	9.9	7.3	7.5	6.6	6.5	7.5	8.1

Monthly Statistical Highlights

	March 1989	April 1989	May 1989
Payroll Employment		+200,000	+227,000
Index of Hours Worked		+0.2%	+0.1%
Household Employment		+207,000	+254,000
Civilian Unemployment Rate		5.1%	5.0%
Personal Income	-0.1%	+0.6%	+0.5%
Savings Rate	5.5%	5.2%	5.3%
Personal Consumption	+0.4%	+1.0%	+0.5%
Retail Sales		+1.6%	+0.2%
Auto Sales		10.5*	10.2*
Housing Starts		-3.1%	-1.8%
Housing Permits		+1.3%	-0.1%
Construction Expenditures	-1.9%	-2.6%	-1.4%
Business Inventories	+0.4%	+0.5%	+0.5%
Orders for Durable Goods	+1.5%	-0.5%	-0.4%
Orders for Nondefense Capital Goods	+4.7%	-3.9%	-0.6%
Industrial Production		+0.2%	+0.2%
CPI		+0.9%	+0.6%
PPI		+0.7%	+0.4%
Consumption Deflator	+0.4%	+0.5%	+0.5%
Leading Indicators	-0.3%	-0.4%	+0.2%
Currency Index		+0.7%	-1.2%
Equity Index		+3.4%	-2.6%
Real GNP (annual rate)	+2.4%	+0.3%	-0.9%
M1 (annual rate)		-2.7%	+2.5%
M2 (annual rate)		+3.6%	+5.2%

* auto sales in millions

Commentary

Employment - The March employment report indicated that economic activity remained sluggish. The index of hours worked showed minimal increase while construction employment fell by 50,000. Thus, weakness in housing starts and in industrial production was appropriately anticipated by the employment report. However, the unemployment rate was not reversed. In fact, a 0.3 percentage point decline in the unemployment rate of adult males caused overall unemployment to fall to 5.0%. A significant slowing in the labor force caused this dip in unemployment. Apparently, less than 200,000 growth in payroll employment will be sufficient to sustain the unemployment rate. In order to create some slack in the labor markets, growth would have to slow significantly.

Thus, hourly earnings probably will continue to exert upward pressure until the economy has slowed to a rate even below the Federal Reserve target range. Moreover, the unemployment rate probably will slide further, although some increase in April appears to be likely.

Hourly earnings grew more than 4.5% at annual rates in March but only increased at a 3.9% annual rate over the past three months. Further acceleration is anticipated in that area. Although the diffusion index did not show recessionary behavior, only 57% of all industries reported employment gains, a figure usually associated with only sluggish growth.

Personal Income and Outlays - Farm subsidies should weaken in March. In addition, the slow growth in payroll employment should generate only a 0.6% increase in wage earnings. Although interest income should continue to grow rapidly, overall personal income could be unchanged in March. The savings rate almost certainly will not be up as sharply as in February, when rising farm subsidies substantially added to personal savings. However, savings in excess of 5% should persist through much of this year.

March retail sales were exceptionally sluggish, as only food and gasoline showed any appreciable increase. These certainly reflected price increases during the month. However, the seasonal adjustments for an early Easter are notoriously unreliable. Typically, sales are expected to be the same on Easter week whether it is early or late. However, more sales normally occur on a late Easter than on an early Easter. For that reason, the seasonal adjustment factors tend to understate retail sales for an early Easter and then overstate them the next month. That pattern appears to be developing again this year. Also, the automobile incentives are having some effect on auto sales in April. Although price concessions are generating the sales, the elasticities are substantially greater than one. Thus, some dollar increases should be anticipated. Coupled with dramatic increases in gasoline prices and continued modest increases in food prices, a substantial surge in nondurable sales is anticipated. Further declines are possible in non-auto durables, especially as home remodeling and household furnishings could be weakening. Nevertheless, retail sales should show a sharp improvement from relatively sluggish March levels.

If the surge in retail activity develops, consumer spending should rebound sharply in April and during the second quarter. After minimal growth in consumer spending during the first quarter, consumption could grow about 2.5% after adjustment for inflation in the second quarter.

Construction - The drop in housing permits during March was widespread and suggests that housing starts will be well under 1.4 million for the remainder of this year. Indeed, if permits do not rebound in April, they will be consistent with single-family starts of less than 950,000. Multi-family starts also appear to be well under 400,000. Slower housing activity should begin developing as early as March with some weakness anticipated in the nonresidential area as well. Construction spending is expected to dramatically slow over the next six months. On the other hand, construction spending in February was surprisingly strong. Perhaps a significant downward revision in that data may develop.

Although the construction cost index rose slightly in February, it has moved little over the past six months. Some acceleration is anticipated later in the year, but weakness in housing activity almost assures that construction material prices will not be rising. Moreover, construction workers probably will have relatively modest wage increases in this recessionary environment.

Business Activity - Although hours worked in durable goods industries suggest little improvement in durable goods orders, large orders for commercial aircraft and a buildup in orders for primary metals in anticipation of work stoppages later in the year should generate a rebound in that area after two monthly declines. The gap between orders and shipments for nondefense capital goods is so large that a significant expansion in shipments should persist the entire year. As a result, capital spending programs almost certainly will be growing 6% to 7% in real terms.

The one surprise in business activity was the two consecutive months of no change in industrial production. Auto assemblies are at 7.1 million units, about in line with sales when incentives are in place. Some further declines should occur in the summer but not before. Industrial material production almost certainly will rise, especially as copper and steel try to stockpile prior to difficult labor negotiations. Capacity utilization has slipped from previous peaks, causing relief from inflation fears. Such relief clearly is justified, but lags in response to slowing economic activity are too long to provide relief as quickly as financial markets currently expect.

Prices - A surge in gasoline prices will dramatically effect the CPI and will also have a moderate effect upon the PPI for finished goods in April. Indeed, both indices almost certainly will be growing more rapidly than in March. The consumer deflator also should show a significant leap upward while prices of consumer nondurables should surge.

Miscellaneous - Even without higher oil prices, the merchandise trade balance would have difficulty significantly declining. Strong growth in capital spending, where 35% of all spending is produced abroad, and the capacity constraints of export-oriented industries assures a dramatic slowing in the improvement in trade balances. When oil price increases are added, deterioration even further than currently projected is possible. Indeed, a shift to $18 oil in April and 260 million barrels could cause the trade deficit in that month to balloon in excess of $12 billion.

The leading indicators almost certainly will now be dropping as a result of this sharp decline in building permits, although orders may blunt the degree of decline. Certainly, falling equity values will also be adding to the decline in leading indicators. Equity prices rebounded in April as a result of diminishing inflationary fears. As indicated above, these easing fears are not justified and the equity markets should soon readjust for that inappropriate anticipation.

Corporate profits should hold up nicely during this period of accelerating inflation, but a significant portion of the gains will be in the petroleum industry. The increased concentration of profits is not as favorable as a broader-based growth of profitability. This also should put downward pressures upon equity values. The currency index may temporarily slip as a result of lessening inflationary fears at home along with tightening monetary policy abroad. However, when bad inflation numbers are again reported in the next few months, the index should again firm. The dollar then would start to fall under unfavorable trade balances and economic weakening later in the year.

It should also be noted that a significant surge in IVA associated with sharp increases in prices of energy materials should now be anticipated. This could lead to inappropriate profit earnings and an incorrect evaluation of inventories as a result of the surge in inventory profits. Initially, stock market values are unable to determine the deteriorating quality of earnings. By summer, however, such a deterioration should be obvious to most analysts.

Financial Markets

Household savings are continuing to grow as a result of the rebound in farm income and sharp growth in interest income. There may also have been a shift in the desired savings schedule. However, household savings are not expected to grow significantly from here.

The government sector is expected to continue running deficits in the $165 billion range for the next several months. Some lessening in those government deficits are likley later in the year, especially after the beginning of the next fiscal year as a result of restraints in defense spending. Next year's deficits should be in the vicinity of $145 billion. Thus, some moderation in government needs for funds could aid in a slight easing of interest rate pressures later this year.

Unfortunately, the surge in the IVA means a significant increase in corporate borrowings for inventory purposes. These borrowing pressures should become substantial late in the spring and early in the summer months. If so, credit market pressures could intensify signficantly. Corporate cash flows still are strong, but the rise in interest borrowings probably will exceed the growth in cash flow. Thus, increased corporate borrowings from the credit markets appear to be likely later in the quarter. This should also coincide with an unexpected surge in loan activity at banks. If so, some further upward pressures upon interest rates should be anticipated within the next few months.

Currently, foreign investors are reassessing their desires to provide funds to the U.S. markets. The dollar may have reached a peak at 1.90 D-mark. Furthermore, interest rate differentials are narrowing. This could create reduced capital flows from foreign investors. If so, the next quarterly funding could be surprisingly poorly supported by foreign investors. Such an outcome could lead to another May massacre in the long-term government bond. At any rate, upward pressures by the corporate sector and diminished attractiveness of American assets by foreign investors should lead to some upward pressures on interest rates late in the spring and in the early summer months. Economic weakness then could generate reduced corporate borrowing needs and a lessening of short-term interest rate pressures before the end of the year.

Equity Markets - The equity markets currently are anticipating the best of all worlds. While corporate profitability is expected to remain high, Federal Reserve restraint is expected to head off wage demands before they intensify. As a result, the profit margin-enhancing programs that have temporarily increased corporate profitability are assumed to remain intact. This wishful thinking certainly will not be realized. Therefore, if interest rates rise again, as anticipated here, the stock market is vulnerable to a significant downside correction. The increase in program trading merely increases the volatility of the market. Indeed, patterns similar to the summer of 1987 appear to be developing in stock market trading. No one is concerned because the increased volatility currently is on the upside.

Although oil servicing companies should be accumulated and some of the holders of oil reserves also should do well in the economic environment that currently is developing, a significant correction in the equity markets currently is anticipated. Thus, significant profit-taking probably will prove to be beneficial at the present time.

EMPLOYMENT

	Payroll Employment		Index of Hours Worked		Household Civilian Employment		Civilian Unemployment Rate		Hourly Earnings	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	106973	106973	127.1	127.1	115573	115573	5.3	5.3	9.43	9.43
November	107377	107419	127.0	127.1	115947	115947	5.4	5.4	9.42	9.42
December	107656	107641	127.1	127.2	116009	116009	5.3	5.3	9.44	9.45
January 1989	108026	108065	127.6	128.3	116435	116711	5.3	5.4	9.50	9.49
February	108277	108345	128.0	127.8	116700	116853	5.2	5.1	9.55	9.50
March	108526	108525	128.4	127.9	116965	117136	5.2	5.0	9.60	9.54
April	108753	108725*	128.7	128.2*	117168	117343*	5.1	5.1*	9.63	9.58*
May	108960	108952	129.0	128.4	117381	117597	5.0	5.0	9.66	9.61
June	109165	109150	129.2	128.6	117592	117811	5.0	5.0	9.68	9.66
July	109328	109376	129.4	128.9	117746	118050	5.0	4.9	9.72	9.70
August	109555	109574	129.7	129.1	117980	118243	5.0	4.9	9.77	9.73
September	109784	109715	129.9	129.2	118221	118409	4.9	4.9	9.81	9.77
October	109938	109828	130.0	129.3	118403	118529	4.9	4.9	9.85	9.82
November	110037	109979	130.2	129.5	118559	118701	4.9	4.8	9.90	9.86
December	110235	110111	130.3	129.6	118716	118837	4.9	4.8	9.95	9.90
January 1990	110423	110185	130.6	129.6	118914	118914	4.8	5.0	9.99	9.94
February	110617	110327	130.8	129.7	119151	119070	4.8	5.1	10.04	9.99
March	110809	110468	131.1	129.8	119362	119211	4.9	5.1	10.09	10.03

PERSONAL INCOME

	Personal Income		Wage & Salary		Personal Savings		Disposable Income		Personal Outlays	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	4.184	4.178	2.512	2.508	182.9	174.0	3.587	3.583	3.404	3.409
November	4.175	4.170	2.520	2.516	153.3	150.1	3.577	3.573	3.423	3.423
December	4.196	4.201	2.522	2.530	157.6	150.4	3.598	3.600	3.440	3.449
January 1989	4.223	4.273	2.543	2.550	167.9	198.3	3.620	3.660	3.452	3.462
February	4.272	4.315	2.571	2.573	189.6	219.6	3.664	3.700	3.474	3.480
March	4.320	4.313*	2.599	2.588*	206.3	203.5*	3.702	3.696*	3.496	3.493*
April	4.343	4.341	2.608	2.606	200.6	194.4	3.719	3.720	3.518	3.526
May	4.366	4.364	2.617	2.620	196.7	198.5	3.734	3.741	3.537	3.543
June	4.389	4.392	2.626	2.639	197.3	206.7	3.750	3.765	3.553	3.558
July	4.412	4.420	2.645	2.658	197.1	213.7	3.773	3.790	3.576	3.576
August	4.434	4.441	2.665	2.671	199.8	205.6	3.797	3.807	3.597	3.601
September	4.456	4.465	2.686	2.686	201.8	205.1	3.820	3.827	3.618	3.622
October	4.479	4.490	2.699	2.703	195.3	208.5	3.835	3.848	3.640	3.639
November	4.501	4.514	2.712	2.720	192.7	204.3	3.852	3.868	3.659	3.664
December	4.523	4.536	2.725	2.734	191.1	198.4	3.868	3.886	3.677	3.688
January 1990	4.552	4.547	2.744	2.747	194.2	191.7	3.895	3.899	3.701	3.707
February	4.582	4.574	2.764	2.764	202.5	194.9	3.926	3.925	3.724	3.730
March	4.613	4.598	2.785	2.779	209.4	200.4	3.953	3.946	3.744	3.746

Fore. = February Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

CONSUMPTION

	Personal Consumption Fore.	Personal Consumption C.E.	Durables Fore.	Durables C.E.	Nondurables Fore.	Nondurables C.E.	Services Fore.	Services C.E.	Consumption Real Fore.	Consumption Real C.E.
October 1988	3302.9	3307.0	452.0	453.3	1071.3	1071.3	1778.8	1782.4	2613.6	2616.9
November	3321.6	3320.3	453.6	458.7	1077.4	1080.9	1782.6	1780.7	2617.9	2623.5
December	3335.8	3346.0	472.1	480.2	1076.9	1069.4	1795.5	1796.4	2635.4	2634.6
January 1989	3349.1	3357.9	460.7	461.1	1080.5	1088.1	1807.6	1808.6	2628.8	2627.2
February	3371.0	3375.7	463.5	459.7	1085.6	1089.0	1821.9	1827.0	2637.7	2636.6
March	3391.9	3387.6*	466.5	458.9*	1090.8	1092.3*	1834.6	1836.4*	2643.7	2634.9*
April	3414.1	3420.1	470.2	469.8	1097.4	1104.0	1846.5	1846.3	2646.6	2646.7
May	3432.5	3436.4	472.4	466.6	1101.3	1111.9	1858.5	1857.9	2648.5	2646.4
June	3447.4	3451.6	471.6	465.4	1105.5	1116.6	1870.3	1869.6	2647.8	2647.8
July	3470.1	3469.0	474.3	464.8	1113.4	1123.0	1882.4	1881.2	2655.0	2650.1
August	3490.9	3493.4	476.8	471.5	1118.6	1127.6	1895.5	1894.3	2662.8	2658.3
September	3511.4	3513.2	479.3	473.5	1123.9	1133.0	1908.2	1906.7	2670.3	2663.9
October	3532.3	3530.1	481.5	473.9	1130.1	1137.9	1920.7	1918.3	2671.9	2665.3
November	3551.1	3553.7	483.3	479.3	1134.0	1143.3	1933.8	1931.1	2672.0	2672.0
December	3567.9	3576.9	483.3	483.4	1138.0	1149.0	1946.6	1944.5	2672.6	2678.2
January 1990	3591.6	3595.9	486.5	484.5	1146.2	1153.2	1958.9	1958.2	2680.3	2680.7
February	3614.0	3618.1	489.4	487.6	1151.9	1159.0	1972.7	1971.5	2687.0	2687.2
March	3633.8	3633.0	490.2	483.9	1157.5	1164.4	1986.3	1984.7	2691.7	2686.8

RETAIL SALES

	Retail Sales Fore.	Retail Sales C.E.	Non-Auto Durables Fore.	Non-Auto Durables C.E.	Auto (Million Units) Fore.	Auto (Million Units) C.E.	Nondurable Sales Fore.	Nondurable Sales C.E.	Auto Sales Fore.	Auto Sales C.E.
October 1988	136.56	136.56	20.90	20.90	9.8	9.9	85.36	85.36	30.30	30.30
November	137.81	137.87	21.10	21.10	10.2	10.2	85.80	85.80	30.91	30.91
December	138.03	137.86	21.51	21.79	11.7	11.6	85.70	85.24	30.82	30.83
January 1989	138.04	140.04	21.27	22.62	9.9	9.8	86.04	86.23	30.73	31.19
February	138.77	139.26	21.16	22.46	10.3	9.9	86.45	86.37	31.16	30.43
March	139.52	139.42	21.13	22.40	10.7	9.6	86.86	86.63	31.53	30.40
April	140.47	141.61*	21.58	22.28*	10.6	10.5*	87.39	87.56*	31.50	31.77*
May	141.03	141.87	21.57	22.36	10.7	10.2	87.70	88.19	31.76	31.32
June	141.27	142.11	21.65	22.25	10.6	10.3	88.03	88.56	31.59	31.30
July	141.50	142.55	21.88	22.37	10.2	10.2	88.66	89.07	30.96	31.11
August	142.90	143.68	22.24	22.52	10.5	10.5	89.08	89.43	31.58	31.73
September	143.60	144.67	21.99	22.65	10.8	10.8	89.50	89.86	32.11	32.16
October	144.34	144.77	22.38	22.69	10.1	10.1	89.99	90.25	31.97	31.83
November	144.86	145.83	22.23	23.02	10.3	10.2	90.30	90.68	32.33	32.13
December	145.18	146.75	21.80	22.86	10.6	10.4	90.62	91.13	32.76	32.76
January 1990	146.19	147.20	22.33	22.85	10.5	10.4	91.27	91.46	32.59	32.89
February	146.97	148.02	22.56	22.97	10.6	10.5	91.73	91.92	32.68	33.13
March	147.49	148.03	22.70	23.11	10.5	10.1	92.17	92.35	32.62	32.57

Fore. = February Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

CONSTRUCTION

	Housing Starts		Single Family Starts		Housing Permits		Construction Expenditures (Current)		Construction Expenditures (Real)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	1.542	1.532	1.112	1.136	1.516	1.516	407.8	407.7	349.8	349.8
November	1.563	1.567	1.151	1.138	1.517	1.516	411.1	411.5	352.6	353.0
December	1.506	1.577	1.121	1.141	1.502	1.566	408.2	421.0	349.2	360.6
January 1989	1.490	1.678	1.095	1.199	1.473	1.507	410.3	422.8	350.4	363.1
February	1.443	1.476	1.063	1.034	1.416	1.415	409.8	423.0	349.7	362.8
March	1.405	1.397	1.032	0.994	1.372	1.221	409.4	415.1*	348.7	355.7*
April	1.457	1.354*	1.056	0.976*	1.375	1.237*	409.3	404.3	348.0	345.9
May	1.490	1.329	1.084	0.954	1.413	1.235	409.5	398.6	347.3	341.0
June	1.466	1.317	1.055	0.962	1.392	1.206	409.3	397.0	346.6	339.0
July	1.438	1.319	1.037	0.955	1.375	1.229	411.9	397.7	347.9	339.0
August	1.414	1.327	1.025	0.943	1.356	1.243	413.2	399.0	347.8	339.3
September	1.423	1.321	1.011	0.927	1.364	1.235	414.4	398.2	347.7	338.0
October	1.425	1.345	1.020	0.951	1.343	1.246	414.3	401.7	346.7	340.4
November	1.413	1.355	1.012	0.956	1.327	1.262	414.6	402.5	346.1	340.5
December	1.414	1.398	1.018	0.992	1.330	1.295	414.5	406.4	344.8	343.0
January 1990	1.369	1.387	0.984	1.003	1.306	1.273	414.9	407.5	344.0	343.3
February	1.358	1.401	0.976	1.012	1.298	1.296	416.1	408.8	343.9	343.5
March	1.345	1.411	0.968	1.015	1.299	1.305	417.4	408.8	343.5	342.7

	Non-Residential		Public Construction		Residential Construction	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	130.9	130.7	77.9	77.0	199.0	200.0
November	129.7	131.7	80.9	79.2	200.4	200.6
December	128.4	133.9	79.5	85.4	200.3	201.7
January 1989	128.8	136.7	81.0	82.1	200.5	203.9
February	128.4	136.8	80.6	82.7	200.8	203.4
March	127.8	134.2*	81.5	82.3*	200.1	198.6*
April	128.3	133.7	81.7	82.8	199.3	187.8
May	128.8	131.6	82.0	83.4	198.7	183.6
June	129.2	131.7	82.0	83.6	198.1	181.7
July	129.5	132.2	82.5	84.1	199.9	181.4
August	129.8	132.7	82.6	84.5	200.8	181.8
September	130.1	132.5	82.8	84.9	201.5	180.8
October	130.4	133.1	83.0	85.3	200.9	183.3
November	130.6	133.6	83.2	85.0	200.8	183.9
December	130.9	134.2	82.8	85.3	200.8	186.9
January 1990	131.5	134.3	83.5	85.5	199.9	187.7
February	132.3	134.7	84.2	85.8	199.6	188.3
March	133.1	134.9	84.9	85.5	199.4	188.4

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BUSINESS ACTIVITY

	Manufacturers' Inventories		Durable Goods Orders		Non-Defense Capital Goods Orders		Non-Defense Capital Shipments	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	349.4	349.4	122.79	122.79	34.62	34.62	32.69	32.60
November	350.9	351.6	122.77	123.04	35.67	35.83	32.43	32.51
December	352.4	354.2	121.85	132.15	34.23	39.43	32.47	32.68
January 1989	354.3	357.3	123.74	128.48	34.93	40.35	32.96	33.33
February	356.8	359.1	122.19	124.20	33.67	37.06	33.02	33.34
March	359.2	361.3*	122.85	126.06*	33.84	38.80*	33.10	33.92*
April	361.5	363.6	123.75	125.43	34.26	37.29	33.43	34.16
May	363.6	366.9	123.14	124.89	34.05	37.05	33.88	34.12
June	365.8	370.1	123.67	125.13	34.35	37.36	34.25	34.31
July	367.9	373.4	124.51	125.01	34.97	37.15	34.56	34.53
August	369.5	375.8	125.89	126.63	35.37	38.02	34.65	34.79
September	372.3	377.3	125.11	126.17	35.11	37.64	34.47	35.07
October	374.6	379.6	124.48	126.19	34.96	37.85	34.69	35.26
November	376.8	381.2	125.93	126.31	35.22	38.09	34.83	35.43
December	378.9	382.9	126.21	125.53	35.29	37.63	34.98	35.66
January 1990	381.1	384.5	127.72	124.78	35.56	37.46	35.15	35.84
February	382.4	386.6	127.85	124.55	36.42	37.09	35.70	36.05
March	383.7	387.9	127.56	124.67	36.40	37.12	36.28	36.11

	Business Inventories		Defense Shipments		Industrial Production		Capacity Utilization	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	751.4	750.6	8.43	8.43	139.3	139.4	84.0	84.0
November	754.4	753.7	8.55	8.66	139.9	139.9	84.2	84.1
December	755.0	756.7	8.63	10.10	140.2	140.4	84.1	84.3
January 1989	760.6	759.8	8.54	8.73	140.8	141.0	84.3	84.4
February	756.5	763.6	8.51	8.44	141.2	141.0	84.4	84.2
March	772.3	766.9*	8.43	8.52*	141.6	141.0	84.5	84.0
April	775.7	770.3	8.50	8.50	142.3	141.3*	84.8	84.0*
May	779.6	773.9	8.55	8.56	142.7	141.6	84.9	84.1
June	783.4	777.1	8.56	8.55	143.2	141.8	85.1	84.1
July	788.1	780.4	8.53	8.62	143.4	142.1	85.0	84.2
August	792.0	784.6	8.55	8.65	143.2	142.3	84.7	84.2
September	795.8	788.1	8.56	8.63	143.5	142.4	84.7	84.1
October	801.1	792.5	8.59	8.78	143.7	142.4	84.6	83.9
November	806.6	798.6	8.61	8.71	143.8	142.6	84.5	83.9
December	812.1	803.5	8.63	8.70	143.9	142.8	84.4	83.9
January 1990	815.3	809.4	8.60	8.73	144.1	142.7	84.3	83.6
February	818.2	815.3	8.65	8.65	144.3	142.9	84.2	83.6
March	821.1	818.2	8.73	8.71	144.6	143.2	84.2	83.7

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PRICES

	CPI-U (seasonally adjusted)		PPI Finished Goods (seasonally adjusted)		PPI-Industrial Commodities (unadjusted)		Estimated GNP Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	119.9	119.9	109.5	109.3	107.1	107.1	123.4	123.5
November	120.3	120.2	109.8	109.6	107.4	107.5	123.8	124.0
December	120.8	120.6	110.3	110.0	108.1	108.1	124.2	124.4
January 1989	121.2	121.3	110.8	111.1	108.7	109.1	124.5	125.1
February	121.5	121.8	111.1	112.2	109.0	110.0	124.8	125.3
March	121.8	122.4	111.4	112.7	109.1	110.6	125.1	125.8
April	122.4	123.5*	111.8	113.2*	109.7	111.2*	125.6	126.4
May	122.9	124.2	112.1	113.6	110.2	111.5	126.1	127.0
June	123.3	124.7	112.4	113.9	110.6	111.9	126.5	127.5
July	124.0	125.1	112.8	114.2	111.3	112.3	127.0	128.0
August	124.7	125.6	113.3	114.5	111.8	112.6	127.4	128.5
September	125.4	126.0	113.9	114.9	110.5	110.9	127.8	128.9
October	125.9	126.4	114.4	115.6	111.8	113.5	128.4	129.4
November	126.3	126.9	114.8	115.9	112.1	114.0	128.9	129.9
December	126.7	127.5	115.1	116.3	112.4	114.4	129.5	130.5
January 1990	127.3	128.0	115.6	116.4	113.0	114.6	129.9	131.0
February	127.9	128.5	116.3	116.6	113.6	114.8	130.3	131.5
March	128.5	129.1	117.0	116.9	114.1	115.1	130.7	132.0

	Consumption Deflator		Consumer Durables		Consumer Nondurables		Consumer Services		Implicit Construction Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	126.4	126.4	111.0	111.1	118.4	118.4	136.8	136.8	116.6	116.6
November	126.6	126.6	111.1	111.1	118.2	118.2	137.3	137.3	116.6	116.6
December	126.9	127.0	111.8	112.0	118.4	118.4	137.8	137.9	116.9	116.7
January 1989	127.4	127.8	112.0	111.8	118.6	119.2	138.4	138.9	117.1	116.4
February	127.8	128.0	112.3	111.7	118.7	119.5	138.9	139.1	117.2	116.6
March	128.3	128.6*	112.6	111.9*	119.4	120.0*	139.3	139.7*	117.4	116.7*
April	129.0	129.2	112.9	112.1	120.2	121.1	140.0	140.3	117.6	116.9
May	129.6	129.9	113.1	112.4	120.9	121.7	140.8	141.0	117.9	116.9
June	130.2	130.4	113.3	112.7	121.5	122.1	141.5	141.6	118.1	117.1
July	130.7	130.9	113.7	113.0	121.8	122.5	142.1	142.3	118.4	117.3
August	131.1	131.4	114.1	113.3	122.0	122.9	142.7	143.0	118.8	117.6
September	131.5	131.9	114.5	113.5	122.3	123.3	143.3	143.6	119.2	117.8
October	132.2	132.4	114.8	113.9	123.0	123.7	144.0	144.3	119.5	118.0
November	132.9	133.0	115.1	114.2	123.8	124.2	144.7	145.0	119.8	118.2
December	133.5	133.6	115.4	114.5	124.6	124.7	145.4	145.7	120.2	118.5
January 1990	134.0	134.1	115.7	114.8	124.9	125.2	146.0	146.4	120.6	118.7
February	134.5	134.6	116.0	115.2	125.1	125.6	146.7	147.0	121.0	119.0
March	135.0	135.2	116.3	115.5	125.4	126.0	147.4	147.7	121.5	119.3

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MISCELLANEOUS

	Merchandise Trade Balance		Leading Indicators	Estimated GNP		Estimated GNP (1982 $)		IVA (annual rate)	
	Fore.	C.E.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	-8.88	-8.88	143.9	4963	4970	4022	4024	-24.4	-20.6
November	-10.18	-10.38	143.9	4984	5001	4026	4033	-20.7	-18.7
December	-9.96	-10.92	144.9	5023	5033	4044	4046	-20.6	-18.3
January 1989	-10.26	-8.67	145.7	5066	5092	4069	4070	-20.1	-20.5
February	-10.72	-10.49	145.2	5085	5112	4075	4080	-21.4	-24.6
March	-10.35	-10.96*	144.8*	5120	5143	4093	4088	-22.7	-27.3
April	-10.11	-10.73	144.0	5153	5169	4103	4089	-21.9	-31.2
May	-10.01	-10.55	144.3	5186	5189	4113	4086	-21.5	-33.5
June	-9.86	-10.26	144.1	5219	5228	4126	4100	-21.3	-27.6
July	-9.95	-9.75	144.3	5237	5265	4124	4113	-25.9	-22.4
August	-9.81	-10.07	144.0	5258	5285	4127	4113	-28.3	-19.3
September	-9.65	-10.23	143.7	5279	5321	4131	4128	-31.0	-15.4
October	-9.55	-9.72	142.3	5305	5347	4132	4132	-27.6	-12.6
November	-9.94	-9.65	142.8	5334	5376	4138	4139	-25.3	-12.9
December	-10.28	-9.43	142.1	5362	5405	4141	4142	-23.1	-16.3
January 1990	-9.79	-9.72	142.3	5390	5440	4149	4153	-29.6	-20.4
February	-9.71	-10.01	142.6	5417	5461	4157	4153	-31.3	-21.2
March	-9.64	-9.56	142.2	5445	5483	4166	4154	-33.0	-20.5

	Currency Index		Adjusted Profits		30-Year Government Bonds		New York Composite	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	95.10	95.10	185.4	190.5	8.89	8.89	156 36	156.36
November	91.91	91.91	186.9	189.6	9.02	9.02	152.67	152.67
December	92.65	91.88	177.3	202.8	9.01	9.01	155.34	155.35
January 1989	95.43	95.12	182.2	211.3	8.92	8.93	158.53	160.40
February	97.22	95.77	181.1	207.6	9.03	9.01	161.46	165.08
March	96.25	96.99	179.9	204.3	9.04	9.17	161.06	160.38
April	94.43	97.43*	178.5	200.6	8.86	9.15*	163.49	165.76*
May	93.36	96.25	177.2	197.3	8.73	9.17	162.25	161.46
June	92.71	98.55	175.8	200.5	9.02	9.32	158.07	160.44
July	92.43	98.82	171.2	201.4	9.38	9.36	154.62	159.47
August	92.00	96.67	169.3	197.3	9.53	9.20	151.72	157.93
September	91.66	97.13	167.6	200.2	9.51	9.07	148.85	161.64
October	90.43	96.24	166.8	196.6	9.63	8.83	150.25	162.08
November	86.55	94.63	165.5	197.4	9.69	8.86	149.53	161.19
December	86.92	94.55	164.5	193.3	9.83	8.82	148.86	156.91
January 1990	90.43	92.73	160.2	194.5	9.80	8.69	145.79	159.40
February	91.67	91.85	156.5	189.6	9.79	8.75	144.81	153.06
March	90.25	90.47	153.3	187.2	9.75	8.71	143.78	150.74

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FINANCIAL MARKETS

	Monetary Base		M1		M2		Federal Funds		T-Bills (6 Mos.)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	283.3	283.8	783.5	785.4	3037.5	3042.2	8.30	8.30	7.50	7.50
November	285.0	284.6	783.6	786.6	3054.0	3059.3	8.35	8.35	7.76	7.76
December	285.0	285.0	787.5	790.2	3066.2	3069.3	8.76	8.76	8.24	8.24
January 1989	288.6	287.9	789.3	786.3	3075.3	3065.7	9.02	9.12	8.38	8.36
February	291.3	287.5	791.2	787.4	3084.7	3070.0	9.15	9.36	8.53	8.55
March	294.0	288.7	793.1	786.5	3093.2	3081.1	9.24	9.85	8.62	8.85
April	295.2	289.0*	800.2	784.7*	3120.6	3090.2*	9.27	9.83*	8.65	8.62*
May	296.1	290.5	809.5	786.3	3143.2	3103.4	9.23	10.17	8.63	8.63
June	297.0	291.8	818.0	789.2	3166.5	3117.5	9.25	10.26	8.55	8.81
July	298.9	293.1	816.5	791.6	3180.2	3130.2	9.68	10.34	8.76	8.84
August	300.7	294.8	817.6	795.9	3193.1	3146.5	9.79	10.35	8.93	8.82
September	302.5	296.5	818.9	800.8	3207.3	3161.5	9.84	10.26	9.02	8.65
October	304.1	298.2	823.2	805.7	3223.5	3176.3	10.13	10.14	9.15	8.49
November	305.3	300.1	826.8	810.9	3246.1	3192.1	10.23	10.05	9.18	8.26
December	306.5	301.7	830.4	814.9	3269.0	3205.7	10.36	9.78	9.20	8.17
January 1990	308.5	303.4	836.3	819.2	3291.5	3220.2	10.35	9.72	9.17	8.02
February	310.3	305.0	842.8	822.9	3306.8	3233.1	10.38	9.63	9.15	7.98
March	312.1	306.6	848.9	827.5	3320.7	3245.6	10.34	9.52	9.12	7.95

	Aaa (Seasoned)		Municipals (Bond Buyer)		(3 Month) Commercial Paper		90 Day CD's		Prime Rate	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	9.51	9.51	7.47	7.47	8.24	8.24	8.36	8.36	10.00	10.00
November	9.45	9.45	7.46	7.46	8.66	8.66	8.78	8.78	10.05	10.05
December	9.57	9.57	7.61	7.61	9.11	9.11	9.25	9.25	10.50	10.50
January 1989	9.58	9.62	7.43	7.35	9.05	9.04	9.15	9.20	10.50	10.50
February	9.50	9.64	7.38	7.44	9.20	9.37	9.29	9.51	10.50	10.93
March	9.46	9.80	7.35	7.59	9.26	9.95	9.35	10.09	10.50	11.50
April	9.40	9.83*	7.31	7.62*	9.38	9.91*	9.43	10.02*	10.50	11.50*
May	9.47	9.86	7.40	7.65	9.35	10.13	9.45	10.24	10.50	11.76
June	9.54	10.02	7.52	7.86	9.40	10.32	9.49	10.40	10.50	12.00
July	9.83	10.05	7.73	7.90	9.65	10.35	9.76	10.43	11.00	12.00
August	9.92	9.87	7.80	7.81	9.76	10.31	9.84	10.40	11.00	12.00
September	10.01	9.53	7.88	7.65	9.86	10.22	9.93	10.36	11.39	12.00
October	10.20	9.46	7.96	7.60	10.15	10.07	10.24	10.20	11.58	12.00
November	10.36	9.49	8.11	7.62	10.24	10.02	10.35	10.11	12.00	12.00
December	10.25	9.52	8.20	7.65	10.35	9.86	10.46	10.01	12.00	12.00
January 1990	10.25	9.39	8.12	7.43	10.33	9.74	10.44	9.86	12.00	11.63
February	10.22	9.44	8.05	7.46	10.36	9.65	10.47	9.79	12.00	11.50
March	10.17	9.40	8.01	7.40	10.38	9.59	10.49	9.71	12.00	11.50

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ECONOMIC FORECASTING CENTER

MONTHLY PROJECTIONS
April 1989

Dr. Donald Ratajczak, Director
For Release: May 23, 1989

STRONG DOLLAR INDICATES THAT FED IS TOO TIGHT

The surge in commodity inflation early in 1989 clearly exceeded Federal Reserve and other analysts' expectations. As a result, the Federal Reserve has moved toward substantial restraint in recent months. Between January and our May estimate, the monetary base has increased at an annual rate of only 2%. M1 has actually declined by 2.5% at annual rates although liquidation of some thrift assets and deposits has contributed to that. However, M2, which is not as significantly impacted by shrinkage in the thrift industry has increased only an annualized 1.2%. If growth in the monetary aggregates has any impact upon economic conditions, this dramatic slowing has significant implications for future economic conditions.

Initially, Federal Reserve restraint was tilting against the wind of significant economic growth. Capacity utilization was rising, reaching a peak of 84.3% in January. As a result, Federal Reserve restraint was accompanied by significant increases in short-term interest rates. The federal funds rate increased by a full percentage point from December through March. Although long-term interest rates also increased, investors viewed the Federal Reserve restraint as necessary to prevent inflation from intensifying. Thus, the long-term bond increased only from a yield of 9.01% in December to 9.17% in March.

Recent statistics show that the combination of unusual weather patterns and early Federal Reserve restraint led to an actual drop in industrial activity during February. This slowing of industrial activity led to moderation in the growth of industrial prices and some weakening of commodity inflation excluding energy. Unfortunately, a combination of minor energy disruptions and a significant lag in response of petroleum product prices to previous increases in prices

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for crude petroleum screened this moderation in industrial inflation from the monetary authorities. With no clearcut evidence that commodity inflation has begun to unwind, the Federal Reserve has continued to "stay the course".

Unfortunately, the Federal Reserve appears to be falling into the same trap that has plagued monetary policy in previous eras. They perceive that staying the course means maintaining prevailing rates of interest. However, the slowing in industrial activity along with moderation in industrial inflation excluding oil has begun reducing the demand for money. The result has been an actual decline in monetary aggregates. In other words, the Federal Reserve currently is more restrained than earlier in the year, the time when restraint was appropriate.

Also, excusing the collapse in checkable deposits as a side effect of the liquidation of deposits at some thrifts may be understating the economic impact that those declining deposits are exerting upon economic conditions. Some of the growing desire to save by consumers may be related to economic concerns arising from the thrift crisis. Despite strong income growth, real consumer spending has been trending downward since January. This has occurred despite auto financing incentives that have largely removed the interest restraint from sales in that sector.

Of course, the strongest signs that monetary policy has become too restrained in the United States and is becoming increasingly restrictive is the surge in the dollar's value. Since December, the trade-weighted value of the dollar has increased 7.7% and has risen by nearly 10% against the German mark and the Japanese yen in the past two months. Although, rising short-term interest rates clearly raised the attractiveness of the dollar, and success with higher interest rates led to greater foreign capital flows into American assets, the latest surge in the dollar has occurred despite a modest narrowing of interest rate differentials. A reduction in merchandise trade deficits also has aided the dollar's strength, but no one ever said that economic experiments can be totally purified. Until monetary restraint eases, the dollar should continue to increase in value.

This has a positive and a negative effect upon economic conditions in the United States. The positive effect clearly is a substantial slowing of inflationary pressures. Imported goods are already beginning to decline in price, with the exception of oil. Further price increases for industrial materials in the United States will be difficult. Indeed, continuation of the dollar's strength could lead to a replay of 1985 in the industrial sector. However, unlike 1985, when consumer spending was strong and construction was still rebounding, those sectors also are weakening. Therefore, the negative impact of a strengthening dollar is a significant decline in economic activity next year.

Some Federal Reserve easing is anticipated, suggesting that bond prices have peaked. However, the Federal Reserve probably will not move aggressively until prior to the Economic Summit, which is scheduled for mid-July. Certainly, the U.S. does not want to enter that economic summit with an appreciating dollar.

Unfortunately, the Federal Reserve probably already has stayed too tight too long. As a result, economic activity is expected to slow significantly late this year and early next year. This should lead to a further downward movement in both short-term and long-term interest rates early in 1990.

Quarterly Profile of GNP

	1989-1	1989-2	1989-3	1989-4	1990-1	1990-2	1989 Annual	1990 Annual
Real:	5.5	0.8	1.8	1.3	1.4	-0.9	2.7	0.8
Price:	3.9	5.1	5.0	4.5	4.6	5.4	4.7	5.2
Nominal:	9.6	6.0	6.9	6.0	5.8	4.5	7.5	6.1

Monthly Statistical Highlights

	April 1989	May 1989	June 1989
Payroll Employment		+201,000	+230,000
Index of Hours Worked		-0.7%	+0.2%
Household Employment		+216,000	+254,000
Civilian Unemployment Rate		5.2%	5.2%
Personal Income	+0.8%	+0.2%	+0.5%
Savings Rate	6.6%	6.2%	6.0%
Personal Consumption	+0.5%	+0.6%	+0.5%
Retail Sales		+0.7%	+0.2%
Auto Sales		10.5 *	10.1 *
Housing Starts		+3.0%	-1.3%
Housing Permits		-1.9%	+1.1%
Construction Expenditures	-1.2%	+0.2%	-0.4%
Business Inventories	+0.4%	+0.5%	+0.5%
Orders for Durable Goods		-0.2%	+0.4%
Orders for Nondefense Capital Goods		-1.1%	+0.8%
Industrial Production		+0.2%	+0.1%
CPI		+0.6%	+0.4%
PPI		+0.6%	+0.4%
Consumption Deflator	+0.8%	+0.4%	+0.5%
Leading Indicators	+0.6%	+0.1%	0.0%
Currency Index		+1.5%	+0.3%
Equity Index		+2.7%	+1.3%
Real GNP (Annual Rate)	+0.6%	+3.3%	-0.3%
M1 (Annual Rate)		-4.9%	+8.0%
M2 (Annual Rate)		-1.6%	+7.1%

* auto sales in million units

Commentary

Employment - April's employment release was another confusing affair. Payroll employment was up only 117,000 and household employment actually declined because of a more than 100,000 decline in agricultural workers. This certainly led to a significant increase in the unemployment rate. However, the hours worked increased sharply. The reported reason for this was the absence of Easter holiday distortion, which the seasonal values partially assumed. If so, the workweek will slip significantly next month. A sharp slowing in the dispersion index to an increase of only slightly more than 53% seemed to confirm that economic activity was continuing to weaken. However, industrial production rebounded stronger than would be anticipated by employment in manufacturing, though not by as much as the hours worked in manufacturing. Moreover, initial unemployment claims have begun again to trend downward slightly while the insured unemployment rate has again fallen to 2.0%. This suggests that some strengthening of economic activity should be surfacing.

One partially negative part of the report was a 0.7% increase in the hourly earnings index. However, this was muted slightly by a downward revision in the earnings index for the previous month.

Personal Income and Outlays - As expected, farm subsidies weakened in March and are now down to levels that could be sustained. However, interest income continues to rise sharply, although declining interest rates in May may shrink that $12 billion per month gain. In addition, personal income in March was aided by some accrued transfer payments that were realized. As a result, transfer payments should flatten in April. The dilemma with personal income for April will be with the wage component, which reflects the extended workweek and higher hourly earnings from the employment report. The size of the wage gains will dictate how much of a distortion the employment figures truly were. With such a surge in April, wage activity should flatten in May. One possible surprise could be the sharp increase in tax collections that apparently are being caused by a significant unbundling of previous tax shelters. Although no such dramatic increase in tax liabilities currently is being projected, this could sharply reduce disposable income in April. Of course, a snapback then would be expected in May.

As April weakness in retail sales appears to be inconsistent with the sharp increase in sales of auto units and an only moderate decline in auto prices for April. This could lead to a significant upward revision in the durables component of consumer spending. However, such adjustments were not made. Of more attention is the significant decline occurring in the non-auto durables. The dip in housing activity clearly is generating significant weakness in household furnishings. Further weakness should develop. Also, sharp increases in gasoline prices will be reflected in nondurable sales in April and May.

Our estimates currently show a decline in consumer spending in the second quarter after adjustment for inflation. This will significantly reduce GNP growth for that quarter.

Construction - The March slump in housing permits, especially for multiple units, was reflected in multiple construction activity in April. As the April permits showed a sharp rebound, some rebound probably should be anticipated in multi-family activity for May. Single-family housing rebounded in the Northeast following surprising weakness in previous months. This probably is an aberration and does not reflect a rebound in the single-family housing sector at this time. Although mortgage rates are beginning to fall, consumers typically remain on the sidelines for several months after the housing market begins declining.

The slippage in residential construction, especially in the mulitple area, should lead to significant declines in spending on residential construction in the months ahead. On the other hand, the March dip in public construction was excessive and probably will be followed by a rebound in the next few months. A sharp increase in nonresidential construction was surprising and widespread. Some slowing in commercial and office building still is anticipated in the months ahead.

Sluggish construction activity has led to minimal gains in construction prices in the past few months. As commodity inflation excites greater price increases for some construction components and as some construction workers garner larger wage increases, some acceleration in the construction deflator is expected. Nevertheless, the construction sector will be a restraining factor upon inflation over the next two years.

Business Activity - Slower sales earlier in the year have led to some slowing in business inventories as well. When these are combined with the sharp increase in inventory valuations, inventories after inflation adjustment are growing at a modest rate at this time. This surprisingly rapid adjustment to changing sales conditions may prevent any serious weakening in production in the months ahead.

Durable goods activity continues to perform as strongly as anticipated. Most of the additional orders are in aerospace, where backlogs are so long that new orders have minimal impact upon current-year activity. Nevertheless, the gap between nondefense capital goods orders and nondefense shipments is so large that significant growth in capital spending should be anticipated into 1990.

The rebound in industrial production was stronger than anticipated by the employment report. However, industrial production was revised downward sharply in Februrary and showed no rebound in March. This led to lower capacity utilization than originally projected. As a result of these revisions, industrial activity is not expected to grow as rapidly as in the February forecast. This also means that capacity utilization will not intensify further in the next year. As a result, industrial inflation should gradually diminish its rate of intensity.

Prices - The auto incentives implied in the PPI only partially were apparent in the CPI for April. Probably, the incentives were not as large as the PPI projected. If so, one more significant increase in both inflation indicators should be anticipated next month. Following that, commodity inflation should ease, causing moderation in the PPI and some slowing in the commodity portion of the CPI. However, accelerating wage pressures should lead to higher than forecasted CPI estimates for much of this year and early into next year.

The largest increases in the consumer deflator should be occurring in March and April. Then, inflationary pressures should ease. Similar patterns are anticipated in the GNP deflator.

Miscellaneous - The trade balances improved more than anticipated as a result of strong increases in world demand for American manufactured goods and American grains. This reduction in trade deficits along with significant Federal Reserve scarcity has led to significant acceleration in the dollar's value. As a result, the currency index could reach 100 in the next month. There is no doubt that a sustained value of the dollar in excess of 140 yen and in excess of 2 German marks would lead to some reduction in those trade balances. Such is projected for the months ahead.

Also of note is a significant deterioration in the quality of profits. Our adjusted profits, which reflect profits after eliminating shifts in tax treatment of depreciation and the inventory valuation, deteriorated sharply during the first quarter. Some rebound is anticipated in the spring and early summer. Apparently, the stock market was unwilling to acknowledge deterioration in the quality of profits and has responded favorably to the decline in interest rates. More will be said later, but this suggests some vulnerability in equity values.

The leading indicators probably peaked at 145.9 in January, although they will again approach that peak in the next few months. Despite the shrinkage in the money stock, the leading indicators almost certainly rose in April as a result of improvement in the workweek, initial claims, orders, permits, and stock prices. A further increase in May could be led by stock prices, although a weakening in sensitive prices and a reversal of the hours worked could derail such a positive event.

Most of the sharp increase in the IVA is the result of sharp increases in oil prices. However, the IVA probably will increase further during the second quarter. This leads to an increase in corporate tax burdens that should impact adversely the adjusted profits of corporations. Then, the quality of profits should improve later this year.

Financial Markets

Apparently, the swing in the household sector has been more significant in altering interest rates than originally anticipated. A sharp rebound in household savings significantly added to the household contribution to credit markets in the first quarter. Then, a significant slowing in housing activity led to further net additions by the household sector during the spring. Further moderate contributions from the household sector are anticipated in the summer before the household sector no longer has such a dramatic impact upon credit market pressures.

Even as the household sector was raising savings, the government sector was able to increase revenues. This has led to a significant shrinkage in government deficits in the winter and spring. Indeed, the deficit currently is running at an annual rate of $145 billion. However, those deficits should increase during the second half of the year. No dramatic surge in government borrowings is anticipated next year, but some further modest increase in government deficits should be anticipated.

Initially, the surge in IVA led to significant increases in corporate borrowings. That surge is beginning to crest. Corporations still are borrowing heavily as a result of significant capital spending programs. There should be some lessening in capital spending activity late this year. On balance, however, the corporate sector is increasing its needs for funds, which normally would lead to rising rates of interest. However, the dramatic shift in the household sector along with some moderate improvement in government borrowings has cancelled out the adverse impact from the corporate sector. As a result, the domestic savings and investment activity should be leading to a slight decline in interest rates at the present time followed by modest interest rate firming later this year.

However, the foreign investor once again has led the interest rate charge. This time, the substantial shortage of dollars has led to a surge in the dollar's value against other currencies. As a result, the positive interest rate differential in the United States has been dramatically attracting investor funds from abroad. The result has been a significant downward movement of interest rates. This downward movement in interest rates probably will persist until the dollar stabilizes. If so, interest rates could fall significantly over the next few months. Then, a period of interest rate stability or even a slight rebound in interest rates could be anticipated. However, the dollar's strength almost certainly will lead to reduced improvement in the trade accounts. Therefore, further weakening in economic activity leading to renewed interest rate declines early next year should be anticipated.

Equity Markets - The foreign investor has also been a factor in holding up equity values. As mentioned earlier, corporate profitability is deteriorating in quality. At some point, actual corporate profits also should be declining as wage pressures continue to intensify while revenues begin to weaken under the onslaught of Federal Reserve restraint. Although the financial sector should do quite well and insurance companies may also rebound, there should be significant weakness in the multi-national companies that usually are associated with the Dow along with some consumer-oriented companies. For this reason, the stock market is expected to show a significant downward correction. However, such a correction probably will not develop until the dollar begin declining. Such a decline is not anticipated until the summer. Unfortunately, the stock market currently has the feel of the market in 1987. How ironic, if the market rallies into the summer months and then begins declining again. If so, profit taking clearly will be in order. In the meantime, don't fight the tape or falling interest rates. The signal to start unloading stocks should be when the dollar crests in its upward move.

EMPLOYMENT

	Payroll Employment		Index of Hours Worked		Household Civilian Employment		Civilian Unemployment Rate		Hourly Earnings	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	106973	106973	127.1	127.1	115573	115573	5.3	5.3	9.43	9.43
November	107377	107419	127.0	127.1	115947	115947	5.4	5.4	9.42	9.42
December	107656	107641	127.1	127.2	116009	116009	5.3	5.3	9.44	9.45
January 1989	108026	108065	127.6	128.3	116435	116711	5.3	5.4	9.50	9.49
February	108277	108341	128.0	127.8	116700	116853	5.2	5.1	9.55	9.50
March	108526	108512	128.4	128.1	116965	117136	5.2	5.0	9.60	9.52
April	108753	108629	128.7	129.5	117168	117113	5.1	5.3	9.63	9.59
May	108960	108830*	129.0	128.6*	117381	117329*	5.0	5.2*	9.66	9.62
June	109165	109060	129.2	128.8	117592	117583	5.0	5.2	9.68	9.64
July	109328	109314	129.4	129.1	117746	117840	5.0	5.1	9.72	9.68
August	109555	109530	129.7	129.3	117980	118069	5.0	5.0	9.77	9.73
September	109784	109784	129.9	129.6	118221	118290	4.9	5.0	9.81	9.77
October	109938	109986	130.0	129.8	118403	118533	4.9	5.0	9.85	9.80
November	110037	110170	130.2	130.0	118559	118732	4.9	5.1	9.90	9.84
December	110235	110321	130.3	130.1	118716	118882	4.9	5.1	9.95	9.89
January 1990	110423	110473	130.6	130.2	118914	119044	4.8	5.2	9.99	9.93
February	110617	110498	130.8	130.2	119151	119065	4.8	5.3	10.04	9.97
March	110809	110450	131.1	130.0	119362	119062	4.9	5.4	10.09	10.02

PERSONAL INCOME

	Personal Income		Wage & Salary		Personal Savings		Disposable Income		Personal Outlays	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	4.184	4.176	2.512	2.507	182.9	170.8	3.587	3.580	3.404	3.409
November	4.175	4.165	2.520	2.514	153.3	140.1	3.577	3.568	3.423	3.428
December	4.196	4.201	2.522	2.530	157.6	150.4	3.598	3.600	3.440	3.449
January 1989	4.223	4.272	2.543	2.559	167.9	187.9	3.620	3.659	3.452	3.472
February	4.272	4.316	2.571	2.571	189.6	213.7	3.664	3.701	3.474	3.487
March	4.320	4.350	2.599	2.592	206.3	234.0	3.702	3.729	3.496	3.495
April	4.343	4.386*	2.608	2.630*	200.6	246.3*	3.719	3.760*	3.518	3.514*
May	4.366	4.396	2.617	2.630	196.7	233.9	3.734	3.769	3.537	3.535
June	4.389	4.416	2.626	2.641	197.3	228.5	3.750	3.780	3.553	3.552
July	4.412	4.445	2.645	2.660	197.1	242.2	3.773	3.808	3.576	3.566
August	4.434	4.472	2.665	2.679	199.8	236.7	3.797	3.832	3.597	3.595
September	4.456	4.498	2.686	2.698	201.8	247.0	3.820	3.856	3.618	3.609
October	4.479	4.517	2.699	2.712	195.3	231.6	3.835	3.872	3.640	3.640
November	4.501	4.541	2.712	2.729	192.7	230.3	3.852	3.892	3.659	3.662
December	4.523	4.560	2.725	2.746	191.1	229.1	3.868	3.908	3.677	3.679
January 1990	4.552	4.581	2.744	2.761	194.2	231.7	3.895	3.927	3.701	3.695
February	4.582	4.600	2.764	2.773	202.5	227.4	3.926	3.943	3.724	3.716
March	4.613	4.621	2.785	2.785	209.4	223.0	3.953	3.961	3.744	3.738

Fore. = February Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

CONSUMPTION

	Personal Consumption		Durables		Nondurables		Services		Consumption Real	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	3302.9	3307.7	452.0	453.2	1071.3	1071.3	1778.8	1783.2	2613.6	2617.1
November	3321.6	3325.4	453.6	458.6	1077.4	1080.9	1782.6	1785.9	2617.9	2626.9
December	3335.8	3346.0	472.1	480.2	1076.9	1069.4	1795.5	1796.4	2635.4	2634.6
January 1989	3349.1	3367.8	460.7	469.1	1080.5	1088.9	1807.6	1809.8	2628.8	2634.1
February	3371.0	3383.2	463.5	461.0	1085.6	1093.9	1821.9	1828.4	2637.7	2641.0
March	3391.9	3390.3	466.5	454.3*	1090.8	1098.4	1834.6	1837.6	2643.7	2629.4
April	3414.1	3408.7*	470.2	456.2	1097.4	1105.2*	1846.5	1847.3*	2646.6	2624.5*
May	3432.5	3429.6	472.4	456.5	1101.3	1114.6	1858.5	1858.5	2648.5	2630.7
June	3447.4	3445.5	471.6	453.7	1105.5	1121.6	1870.3	1870.2	2647.8	2628.9
July	3470.1	3459.2	474.3	451.4	1113.4	1125.1	1882.4	1882.7	2655.0	2628.3
August	3490.9	3488.1	476.8	463.0	1118.6	1130.5	1895.5	1894.6	2662.8	2639.0
September	3511.4	3500.2	479.3	456.9	1123.9	1137.0	1908.2	1906.3	2670.3	2639.3
October	3532.3	3531.0	481.5	470.8	1130.1	1141.4	1920.7	1918.8	2671.9	2651.5
November	3551.1	3551.7	483.3	473.9	1134.0	1146.6	1933.8	1931.2	2672.0	2656.5
December	3567.9	3568.2	483.3	472.7	1138.0	1151.2	1946.6	1944.3	2672.6	2658.1
January 1990	3591.6	3584.0	486.5	471.7	1146.2	1155.4	1958.9	1956.9	2680.3	2658.1
February	3614.0	3603.8	489.4	474.4	1151.9	1161.6	1972.7	1967.8	2687.0	2663.7
March	3633.8	3625.6	490.2	477.7	1157.5	1167.7	1986.3	1980.2	2691.7	2669.1

RETAIL SALES

	Retail Sales		Non-Auto Durables		Auto (Million Units)		Nondurable Sales		Auto Sales	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	136.56	136.56	20.90	20.90	9.8	9.9	85.36	85.36	30.30	30.30
November	137.81	137.87	21.10	21.10	10.2	10.2	85.80	85.80	30.91	30.91
December	138.03	137.86	21.51	21.79	11.7	11.5	85.70	85.24	30.82	30.83
January 1989	138.04	140.04	21.27	22.62	9.9	9.8	86.04	86.23	30.73	31.19
February	138.77	139.43	21.16	22.43	10.3	9.9	86.45	86.36	31.16	30.64
March	139.52	139.36	21.13	22.13	10.7	9.6	86.86	86.76	31.53	30.48
April	140.47	139.93	21.58	21.83	10.6	10.8	87.39	87.30	31.50	30.81
May	141.03	140.90*	21.57	22.06*	10.7	10.5*	87.70	88.04*	31.76	30.80*
June	141.27	141.13	21.65	21.92	10.6	10.1	88.03	88.59	31.59	30.62
July	141.50	141.31	21.88	21.76	10.2	10.0	88.66	88.93	30.96	30.51
August	142.90	142.98	22.24	21.83	10.5	10.6	89.08	89.36	31.58	31.79
September	143.60	142.72	21.99	21.99	10.8	10.1	89.50	89.81	32.11	30.92
October	144.34	144.68	22.38	21.87	10.1	10.4	89.99	90.16	31.97	32.65
November	144.86	145.45	22.23	22.00	10.3	10.5	90.30	90.57	32.33	32.88
December	145.18	145.67	21.80	22.23	10.6	10.3	90.62	90.93	32.76	32.51
January 1990	146.19	145.88	22.33	22.06	10.5	10.3	91.27	91.26	32.59	32.56
February	146.97	146.27	22.56	22.14	10.6	10.1	91.73	91.75	32.68	32.38
March	147.49	147.13	22.70	22.33	10.5	10.2	92.17	92.23	32.62	32.57

Fore. = February Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

CONSTRUCTION

	Housing Starts		Single Family Starts		Housing Permits		Construction Expenditures (Current)		Construction Expenditures (Real)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	1.542	1.532	1.112	1.136	1.516	1.526	407.8	407.7	349.8	349.8
November	1.563	1.567	1.151	1.138	1.517	1.508	411.1	411.5	352.6	353.0
December	1.506	1.577	1.121	1.141	1.502	1.518	408.2	421.0	349.2	360.6
January 1989	1.490	1.678	1.095	1.199	1.473	1.486	410.3	418.0	350.4	358.9
February	1.443	1.465	1.063	1.029	1.416	1.403	409.8	414.8	349.7	355.7
March	1.405	1.399	1.032	0.986	1.372	1.230	409.4	413.5	348.7	354.2
April	1.457	1.361	1.056	1.036	1.375	1.318	409.3	408.6*	348.0	349.8*
May	1.490	1.402*	1.084	1.027*	1.413	1.293*	409.5	409.6	347.3	350.1
June	1.466	1.384	1.055	1.007	1.392	1.307	409.3	408.0	346.6	348.4
July	1.438	1.372	1.037	1.011	1.375	1.284	411.9	410.0	347.9	349.5
August	1.414	1.413	1.025	1.034	1.356	1.326	413.2	410.3	347.8	349.5
September	1.423	1.442	1.011	1.056	1.364	1.335	414.4	412.6	347.7	350.9
October	1.425	1.447	1.020	1.049	1.343	1.358	414.3	412.6	346.7	350.3
November	1.413	1.482	1.012	1.073	1.327	1.376	414.6	414.9	346.1	351.6
December	1.414	1.516	1.018	1.102	1.330	1.412	414.5	419.6	344.8	355.0
January 1990	1.369	1.511	0.984	1.100	1.306	1.405	414.9	420.8	344.0	355.1
February	1.358	1.513	0.976	1.093	1.298	1.416	416.1	422.7	343.9	355.8
March	1.345	1.509	0.968	1.085	1.299	1.403	417.4	423.5	343.5	355.6

	Non-Residential		Public Construction		Residential Construction	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	130.9	130.7	77.9	77.0	199.0	200.0
November	129.7	131.7	80.9	79.2	200.4	200.6
December	128.4	133.9	79.5	85.4	200.3	201.7
January 1989	128.8	135.1	81.0	81.4	200.5	201.4
February	128.4	133.7	80.6	81.5	200.8	199.6
March	127.8	138.7	81.5	74.1	200.1	200.7
April	128.3	136.4*	81.7	77.3*	199.3	194.9*
May	128.8	136.9	82.0	80.4	198.7	192.3
June	129.2	137.5	82.0	80.1	198.1	190.4
July	129.5	137.2	82.5	80.6	199.9	192.2
August	129.8	137.0	82.6	81.4	200.8	191.9
September	130.1	136.4	82.8	82.3	201.5	193.9
October	130.4	136.0	83.0	81.5	200.9	195.1
November	130.6	136.3	83.2	82.6	200.8	196.0
December	130.9	136.5	82.8	83.4	200.8	199.7
January 1990	131.5	135.8	83.5	83.0	199.9	202.0
February	132.3	136.2	84.2	84.2	199.6	202.3
March	133.1	136.5	84.9	84.5	199.4	202.5

Fore. = February Forecast
C.E. = Current Expectations
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BUSINESS ACTIVITY

	Manufacturers' Inventories		Durable Goods Orders		Non-Defense Capital Goods Orders		Non-Defense Capital Shipments	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	349.4	349.4	122.79	122.79	34.62	34.62	32.69	32.60
November	350.9	351.6	122.77	123.04	35.67	35.83	32.43	32.51
December	352.4	354.2	121.85	132.15	34.23	39.43	32.47	32.68
January 1989	354.3	357.5	123.74	128.48	34.93	40.35	32.96	33.33
February	356.8	359.1	122.19	124.11	33.67	37.19	33.02	33.46
March	359.2	360.4	122.85	125.21	33.84	38.09	33.10	34.03
April	361.5	362.7*	123.75	123.87*	34.26	38.67*	33.43	34.27*
May	363.6	364.7	123.14	123.65	34.05	38.26	33.88	34.52
June	365.8	366.3	123.67	124.16	34.35	38.55	34.25	34.89
July	367.9	368.8	124.51	125.09	34.97	39.07	34.56	35.16
August	369.5	370.4	125.89	125.11	35.37	38.82	34.65	35.27
September	372.3	372.0	125.11	124.83	35.11	38.51	34.47	35.53
October	374.6	374.6	124.48	124.55	34.96	38.26	34.69	35.89
November	376.8	377.3	125.93	125.13	35.22	38.39	34.83	36.05
December	378.9	380.5	126.21	124.67	35.29	38.06	34.98	36.17
January 1990	381.1	382.7	127.72	123.62	35.56	37.62	35.15	36.02
February	382.4	384.1	127.85	124.46	36.42	38.11	35.70	36.15
March	383.7	386.4	127.56	124.05	36.40	37.76	36.28	36.24

	Business Inventories		Defense Shipments		Industrial Production		Capacity Utilization	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	751.4	750.6	8.43	8.43	139.3	139.4	84.0	84.0
November	754.4	753.7	8.55	8.66	139.9	139.9	84.2	84.1
December	755.0	756.7	8.63	10.10	140.2	140.4	84.1	84.3
January 1989	760.6	759.8	8.54	8.73	140.8	140.8	84.3	84.3
February	766.5	763.6	8.51	8.40	141.2	140.4	84.4	83.9
March	772.3	765.6	8.43	8.50	141.6	140.5	84.5	83.7
April	775.7	768.7*	8.50	8.58*	142.3	141.1	84.8	83.9
May	779.6	772.4	8.55	8.69	142.7	141.4*	84.9	83.9*
June	783.4	776.0	8.56	8.65	143.2	141.6	85.1	83.8
July	788.1	781.2	8.53	8.70	143.4	141.8	85.0	83.7
August	792.0	785.1	8.55	8.73	143.2	142.3	84.7	83.9
September	795.8	789.5	8.56	8.70	143.5	142.6	84.7	83.9
October	801.1	792.9	8.59	8.62	143.7	143.0	84.6	84.0
November	806.6	796.6	8.61	8.69	143.8	143.1	84.5	83.9
December	812.1	800.4	8.63	8.84	143.9	143.2	84.4	83.8
January 1990	815.3	804.7	8.60	8.83	144.1	143.0	84.3	83.5
February	818.2	808.5	8.65	8.75	144.3	142.7	84.2	83.2
March	821.1	812.2	8.73	8.86	144.6	142.3	84.2	82.9

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PRICES

	CPI-U (seasonally adjusted)		PPI Finished Goods (seasonally adjusted)		PPI-Industrial Commodities (unadjusted)		Estimated GNP Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	119.9	120.0	109.5	109.2	107.1	107.1	123.4	123.5
November	120.3	120.3	109.8	109.4	107.4	107.5	123.8	124.0
December	120.8	120.7	110.3	109.9	108.1	108.1	124.2	124.4
January 1989	121.2	121.4	110.8	111.0	108.7	109.1	124.5	125.0
February	121.5	121.9	111.1	112.1	109.0	110.0	124.8	125.2
March	121.8	122.5	111.4	112.6	109.1	110.6	125.1	125.5
April	122.4	123.4	111.8	113.1	109.7	111.3	125.6	126.3
May	122.9	124.1*	112.1	113.8*	110.2	111.9*	126.1	126.7
June	123.3	124.6	112.4	114.2	110.6	112.2	126.5	127.4
July	124.0	125.0	112.8	114.4	111.3	112.4	127.0	127.9
August	124.7	125.5	113.3	114.7	111.8	112.6	127.4	128.4
September	125.4	125.9	113.9	114.7	110.5	111.0	127.8	128.8
October	125.9	126.5	114.4	115.0	111.8	113.0	128.4	129.3
November	126.3	127.0	114.8	115.3	112.1	113.2	128.9	129.8
December	126.7	127.5	115.1	115.6	112.4	113.5	129.5	130.3
January 1990	127.3	128.1	115.6	116.0	113.0	113.9	129.9	130.8
February	127.9	128.6	116.3	116.5	113.6	114.3	130.3	131.2
March	128.5	129.1	117.0	116.8	114.1	114.7	130.7	131.8

	Consumption Deflator		Consumer Durables		Consumer Nondurables		Consumer Services		Implicit Construction Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	126.4	126.4	111.0	111.1	118.4	118.4	136.8	136.7	116.6	116.6
November	126.6	126.6	111.1	111.1	118.2	118.2	137.3	137.4	116.6	116.6
December	126.9	127.0	111.8	112.0	118.4	118.4	137.8	137.9	116.9	116.7
January 1989	127.4	127.9	112.0	112.0	118.6	119.4	138.4	138.9	117.1	116.4
February	127.8	128.1	112.3	111.7	118.7	119.5	138.9	139.2	117.2	116.6
March	128.3	128.9	112.6	111.3	119.4	121.0	139.3	139.9	117.4	116.7
April	129.0	129.9*	112.9	111.6*	120.2	122.8*	140.0	140.4*	117.6	116.8*
May	129.6	130.4	113.1	111.3	120.9	123.5	140.8	141.0	117.9	117.0
June	130.2	131.1	113.3	112.2	121.5	124.1	141.5	141.6	118.1	117.1
July	130.7	131.6	113.7	112.4	121.8	124.5	142.1	142.3	118.4	117.3
August	131.1	132.2	114.1	113.0	122.0	125.0	142.7	143.0	118.8	117.4
September	131.5	132.6	114.5	112.8	122.3	125.4	143.3	143.6	119.2	117.6
October	132.2	133.2	114.8	113.4	123.0	125.9	144.0	144.3	119.5	117.8
November	132.9	133.7	115.1	113.7	123.8	126.3	144.7	145.0	119.8	118.0
December	133.5	134.2	115.4	113.9	124.6	126.7	145.4	145.7	120.2	118.2
January 1990	134.0	134.8	115.7	114.4	124.9	127.1	146.0	146.4	120.6	118.5
February	134.5	135.3	116.0	114.6	125.1	127.5	146.7	147.0	121.0	118.8
March	135.0	135.8	116.3	115.0	125.4	127.9	147.4	147.7	121.5	119.1

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MISCELLANEOUS

	Merchandise Trade Balance		Leading Indicators	Estimated GNP		Estimated GNP (1982 $)		IVA (annual rate)	
	Fore.	C.E.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	-8.88	-8.78	143.9	4963	4970	4022	4024	-24.4	-20.6
November	-10.18	-10.66	144.1	4984	5001	4026	4033	-20.7	-19.3
December	-9.96	-10.99	144.8	5023	5028	4044	4042	-20.6	-20.4
January 1989	-10.26	-8.68	145.9	5066	5109	4069	4087	-20.1	-26.7
February	-10.72	-9.82	145.4	5085	5114	4075	4085	-21.4	-39.6
March	-10.35	-8.86	144.4	5120	5127	4093	4085	-22.7	-41.7
April	-10.11	-9.78*	145.3*	5153	5162	4103	4087	-21.9	-45.3
May	-10.01	-9.55	145.5	5186	5192	4113	4098	-21.5	-42.3
June	-9.86	-9.52	145.5	5219	5220	4126	4097	-21.3	-36.7
July	-9.95	-9.84	145.1	5237	5257	4124	4110	-25.9	-31.6
August	-9.81	-10.17	144.8	5258	5277	4127	4110	-28.3	-27.5
September	-9.65	-10.23	145.0	5279	5301	4131	4116	-31.0	-23.8
October	-9.55	-9.97	144.6	5305	5327	4132	4120	-27.6	-24.6
November	-9.94	-9.76	144.7	5334	5356	4138	4126	-25.3	-28.5
December	-10.28	-8.84	144.9	5362	5383	4141	4131	-23.1	-23.1
January 1990	-9.79	-8.73	144.3	5390	5407	4149	4134	-29.6	-18.9
February	-9.71	-8.21	144.5	5417	5430	4157	4139	-31.3	-21.6
March	-9.64	-8.42	144.2	5445	5453	4166	4138	-33.0	-24.8

	Currency Index		Adjusted Profits		30-Year Government Bonds		New York Composite	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	95.10	95.10	185.4	190.5	8.89	8.89	156 36	156.36
November	91.91	91.91	186.9	190.6	9.02	9.02	152.67	152.67
December	92.65	91.88	177.3	203.3	9.01	9.01	155.34	155.35
January 1989	95.43	95.12	182.2	210.5	8.92	8.93	158.53	160.40
February	97.22	95.77	181.1	163.4	9.03	9.01	161.46	165.08
March	96.25	96.99	179.9	154.4	9.04	9.17	161.06	164.60
April	94.43	97.43*	178.5	159.8	8.86	9.03	163.49	169.38*
May	93.36	98.92	177.2	183.6	8.73	8.86*	162.25	175.26
June	92.71	99.26	175.8	185.2	9.02	8.82	158.07	177.52
July	92.43	97.43	171.2	193.7	9.38	8.69	154.62	171.88
August	92.00	95.67	169.3	190.4	9.53	8.68	151.72	165.35
September	91.66	92.55	167.6	191.6	9.51	8.73	148.85	160.44
October	90.43	93.76	166.8	190.3	9.63	8.55	150.25	163.65
November	86.55	93.16	165.5	191.7	9.69	8.59	149.53	163.03
December	86.92	91.48	164.5	196.5	9.83	8.68	148.86	161.36
January 1990	90.43	91.86	160.2	193.7	9.80	8.54	145.79	161.67
February	91.67	91.24	156.5	190.6	9.79	8.52	144.81	159.46
March	90.25	91.63	153.3	180.8	9.75	8.47	143.78	152.15

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FINANCIAL MARKETS

	Monetary Base		M1		M2		Federal Funds		T-Bills (6 Mos.)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	283.3	283.8	783.5	785.4	3037.5	3042.2	8.30	8.30	7.50	7.50
November	285.0	284.6	783.6	786.6	3054.0	3059.3	8.35	8.35	7.76	7.76
December	285.0	285.3	787.5	790.3	3066.2	3069.3	8.76	8.76	8.24	8.24
January 1989	288.6	287.9	789.3	786.3	3075.3	3065.6	9.02	9.12	8.38	8.36
February	291.3	287.5	791.2	787.4	3084.7	3069.7	9.15	9.36	8.53	8.55
March	294.0	289.4	793.1	786.3	3093.2	3079.5	9.24	9.85	8.62	8.85
April	295.2	290.3*	800.2	782.9	3120.6	3081.7*	9.27	9.84	8.65	8.65
May	296.1	289.8	809.5	779.6*	3143.2	3077.6	9.23	9.77*	8.63	8.33*
June	297.0	292.4	818.0	784.6	3166.5	3095.2	9.25	9.38	8.55	8.04
July	298.9	294.8	816.5	788.5	3180.2	3110.6	9.68	9.26	8.76	7.96
August	300.7	297.1	817.6	792.2	3193.1	3125.2	9.79	9.32	8.93	8.02
September	302.5	300.6	818.9	797.1	3207.3	3144.5	9.84	9.35	9.02	8.04
October	304.1	302.7	823.2	801.7	3223.5	3165.6	10.13	9.39	9.15	8.11
November	305.3	304.9	826.8	805.1	3246.1	3189.0	10.23	9.46	9.18	8.13
December	306.5	306.5	830.4	810.4	3269.0	3209.9	10.36	9.40	9.20	8.10
January 1990	308.5	307.6	836.3	815.3	3291.5	3233.3	10.35	9.23	9.17	7.86
February	310.3	309.3	842.8	820.8	3306.8	3255.1	10.38	9.02	9.15	7.64
March	312.1	311.0	848.9	825.9	3320.7	3275.3	10.34	8.73	9.12	7.39

	Aaa (Seasoned)		Municipals (Bond Buyer)		(3 Month) Commercial Paper		90 Day CD's		Prime Rate	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
October 1988	9.51	9.51	7.47	7.47	8.24	8.24	8.36	8.36	10.00	10.00
November	9.45	9.45	7.46	7.46	8.66	8.66	8.78	8.78	10.05	10.05
December	9.57	9.57	7.61	7.61	9.11	9.11	9.25	9.25	10.50	10.50
January 1989	9.58	9.62	7.43	7.35	9.05	9.04	9.15	9.20	10.50	10.50
February	9.50	9.64	7.38	7.44	9.20	9.37	9.29	9.51	10.50	10.93
March	9.46	9.80	7.35	7.59	9.26	9.95	9.35	10.09	10.50	11.50
April	9.40	9.79	7.31	7.49	9.38	9.81	9.43	9.94	10.50	11.50*
May	9.47	9.54*	7.40	7.22*	9.35	9.56*	9.45	9.72*	10.50	11.50
June	9.54	9.50	7.52	7.13	9.40	9.32	9.49	9.56	10.50	11.17
July	9.83	9.36	7.73	6.98	9.65	9.23	9.76	9.42	11.00	11.00
August	9.92	9.33	7.80	6.95	9.76	9.28	9.84	9.45	11.00	11.00
September	10.01	9.38	7.88	7.02	9.86	9.35	9.93	9.52	11.39	11.00
October	10.20	9.18	7.96	6.79	10.15	9.41	10.24	9.55	11.58	11.00
November	10.36	9.23	8.11	6.86	10.24	9.48	10.35	9.63	12.00	11.00
December	10.25	9.39	8.20	7.03	10.35	9.37	10.46	9.55	12.00	11.00
January 1990	10.25	9.27	8.12	6.92	10.33	9.15	10.44	9.36	12.00	11.00
February	10.22	9.25	8.05	6.89	10.36	8.96	10.47	9.07	12.00	10.76
March	10.17	9.22	8.01	6.87	10.38	8.67	10.49	8.84	12.00	10.50

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C.E. = Current Expectations
* = This item and those beyond it are projections.

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ECONOMIC FORECASTING CENTER

MONTHLY PROJECTIONS
May 1989

Dr. Donald Ratajczak, Director
For Release: Monday, June 12, 1989

WHY ARE INTEREST RATES FALLING, ANYWAY?

Obviously, falling interest rates will lower the financing costs of conducting business. It also should increase demand for housing, consumer durables and other consumables, all other things equal. Of course, if employment and earning prospects are declining, all other things will not be equal and those activities may continue to fall. Thus, a decline in interest rates cannot always be construed as beneficial to the economy, for it may actually reflect developing undersirable conditions. Should we cheer or jeer because interest rates are tumbling down?

Clearly, if the Federal Reserve is responsible for the decline in interest rates, the shift in monetary policy would be a near-term stimulant to the economy. Until the additional economic activity generated by this stimulant led to increasing inflation, the result probably should be cheered. However, the Federal Reserve is not leading interest rates downward. The yield curve is significantly inverted. This alone suggests that substantial liquidity restraints are present in the system. Also, the strong dollar, at least partially is the result of strong money growth in Germany and Japan relative to the United States. Furthermore, the relationship between federal funds rates and the commercial paper rate suggests that credit market demand conditions rather than Federal Reserve monetary conditions are responsible for any dip in short-term interest rates. Indeed, if the Fed continues to drag its feet, it may preside over several months of declining monetary aggregates. This, in turn, would lead to higher dollar values against other currencies and an interest rate that declines more slowly than what would be necessary to re-establish equilibrium in the credit markets. As a result, the economy could deteriorate swiftly.

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Clearly, the Federal Reserve is not responsible for the decline in short-term interest rates at this time. Rather, it is a cause of higher short-term rates than should prevail.

Of course, foreign capital flows may also explain the dip in interest rates. Foreign investors have become confident that dollars will remain relatively scarce in comparison to yen and marks. This has resulted in a significant increase in the dollar's value, leading to substantial appreciation potential for foreign investors. Unquestionably, capital flows from abroad have been responsible both for the increase in stock market values and the significant rally in the government bond markets. Indeed, the fact that government securities, which foreign investors favor, have improved much more dramatically than corporate issues suggests that the foreign element is substantial.

Of course, foreign capital flows are mercurial. If the dollar starts sliding, they can flee as quickly as they came. To the extent that foreign capital flows are responsible for falling interest rates, that limits the degree to which interest rates ultimately can decline.

However, other information suggests that the economy is slowing. The purchasing managers' index fell below 50%, usually associated with the point at which an economy begins expanding. The industrial sector gave up 15,000 jobs in May while our estimates of industrial production show a modest decline for the month. In short, economic activity stagnated this month. This sluggish performance probably is responsible for most of the interest rate declines. Moreover, as the economy is interest-insensitive, relatively small changes in credit market pressures can lead to significant declines in interest rates. Until the dollar begins weakening, interest rates could fall swiftly. Our current projections suggest that the prime rate will reach 10% by next June. More substantial declines would have been projected except for the adverse effects once interest rate declines begin to reduce currency values.

Determining that most of the interest rate decline is the result of economic weakness still does not provide any information about the cause of that weakness. However, GNP revisions for the first quarter provide a significant clue.

According to the GNP report, economic activity was revised downward sharply mostly as a result of a significant decline in inventory investments. That downward revision in inventory accumulations was caused by two factors. First, rising industrial prices, especially petroleum-based materials, caused a higher inventory adjustment than previously anticipated. As a result, actual inventory investments reflected lower accumulations of materials and goods than originally thought. Because those material prices peaked in April, the IVA is now declining. The same quantity of inventories now can be accumulated at a lower finance cost than previously.

Second, manufacturers apparently are beginning to sense that future sales will not be up to previous anticipations. As a result, they are reducing their production schedules in order to adjust inventories to those lower projections. Indeed, most of the inventory gains have been the result of goods in process, usually aircraft, or in automobiles. In the automobile industry, producers thought financing incentives would be more favorably greeted than actually occurred. The result has been an overhang of inventories that now are being adjusted downward with the aid of production curtailments. This minor inventory adjustment probably will run its course during the second quarter. Then, economic activity should rebound modestly in the second half of the year before excess inventories again are accumulated. A dip in economic activity still appears likely early next year.

Nevertheless, a soft landing now appears more likely than previously. In order to achieve such an event, the Federal Reserve would need to significantly increase money growth in the next few months. This would lead to sharper interest rate declines, at least on the short-end of the yield curve. Also, the dollar would fall more significantly. These two events would stimulate industrial activity and prevent any further curtailment of industrial production. However, the Federal Reserve appears to be following an interest rate target and is not likely to engage in such activity.

Quarterly Profile of GNP

	1989-1	1989-2	1989-3	1989-4	1990-1	1990-2	1989 Annual	1990 Annual
Real:	4.3	0.9	2.2	2.2	1.6	0.7	2.6	1.3
Price:	3.9	5.6	4.6	3.9	4.1	4.3	4.8	4.4
Nominal:	8.9	6.6	6.9	6.2	5.9	5.2	7.6	5.8

Monthly Statistical Highlights

	May 1989	June 1989	July 1989
Payroll Employment		+163,000	+332,000
Index of Hours Worked		+0.3%	+0.2%
Household Employment		+165,000	+315,000
Civilian Unemployment Rate		5.3%	5.2%
Personal Income	+0.4%	+0.4%	+0.6%
Savings Rate	5.6%	5.6%	5.7%
Personal Consumption	+0.6%	+0.4%	+0.5%
Retail Sales	+0.8%	-0.1%	+0.3%
Auto Sales	10.5*	10.0*	9.9*
Housing Starts	+2.4%	+1.0%	-0.4%
Housing Permits	-1.0%	+0.5%	-0.8%
Construction Expenditures	-0.3%	-0.4%	-0.4%
Business Inventories	+0.8%	+0.8%	+0.7%
Orders for Durable Goods	-0.3%	-0.9%	+0.2%
Orders - Nondefense Capital Goods	-3.1%	-0.5%	+0.2%
Industrial Production	-0.1%	+0.2%	+0.2%
CPI	+0.6%	+0.5%	+0.4%
PPI		+0.3%	+0.3%
Consumption Deflator	+0.5%	+0.5%	+0.4%
Leading Indicators	-0.6%	+0.2%	-0.4%
Currency Index		+2.1%	-2.1%
Equity Index		+3.8%	+1.0%
Real GNP (annual rate)	-0.3%	+3.6%	+0.9%
M1 (annual rate)	-12.3%	+4.4%	+10.5%
M2 (annual rate)	-3.6%	+6.1%	+7.6%

* auto sales in millions

Commentary

Employment - May's employment release showed weakness. Payroll employment increased only 101,000 while the workweek declined. The decline in the workweek probably reflects the bias that was generated in the previous month's survey. As a result, the index of hours worked fell 0.9%. More significantly, employment in manufacturing fell 15,000. This suggests that industrial production actually weakened during the month. Moreover, initial claims continued to creep up during May while the insured unemployment rate also rose modestly.

The one good factor in the report was virtually no growth in hourly earnings. During the last three months the hourly earnings index increased 3.8% at annual rates and is up 3.7% from a year ago. This suggests that wage inflation remains subdued. Normally, a shrinkage in both hours and employment growth rates would suggest further weakness next month. However, if the hours purely reflect sampling bias, some rebound is possible in June.

Personal Income and Outlays - Excluding bonus payments in the automobile industry and one-time payments of social security, personal income would have increased 0.7% in April following a 0.6% gain in March. However, those factors which bloated the March gains led to a 0.4% April increase. Payroll reports suggest that there should be minimal growth in wage earnings during May. However, normal gains in tranfer and property income should provide some growth in personal income. An unusual spurt in tax collections led to no change in disposable income during April. This spurt appears to be a one-month event and could be associated with reversals of previous tax shelters. If so, a return to more normal tax liabilities and savings rates will develop.

The April measure of durable spending showed greater increases in auto activity than was contained in April retail sales. This suggests that the April retail sales figure will be revised upward. Our May estimates attempt to show what the actual levels of activity will be. Thus, an upward revision in April would lead to a lower gain in retail sales for May than currently reported. Auto sales are weakening slightly as the novelty of financing incentives is wearing thin.

Because of stronger housing activity as a result of declining interest rates than anticipated a month ago, durable goods sales are expected to be slightly stronger than originally projected. Nondurable sales also should be modestly stronger reflecting significant price gains for gasoline. Expenditures on services probably will not reach forecasted values as housing and educational services are growing slower than previously expected.

The surge in automobile purchases in April should generate some real growth in consumer spending for the second quarter. However, the rate of growth is down sharply from other quarters.

Construction - Housing starts in April reflected the housing permits of the previous month. The only surprise was slightly stronger activity for single-family units than would have been suggested. The sharp rebound in permits during April suggests that housing activity could rebound in May. Coupled with the decline in interest rates, the bottom in housing activity may have been reached. While no significant acceleration of housing activity is expected, gradual improvement in both single-family and multi-family activity should be anticipated. According to Department of Commerce estimates, the vacancy rates for rental units in the first quarter fell from 8.1% a year ago to 7.3%. While this still is historically high, apartment construction is growing more slowly than apartment occupancy. Soon, rental rates will begin accelerating, leading to an acceleration in the consumer services deflator. Then, improving apartment activity should be anticipated.

Expected weakness in nonresidential activity was heavily concentrated in shopping malls and other retail outlets. Industrial activity remains strong while office activity is stagnant. Further declines are anticipated in office activity before nonresidential construction bottoms out. However, the rate of decline in construction activity should slow markedly and reach a low point before the end of this year. Public construction rebounded from the March dip, as expected. Moderate growth now should be anticipated in public construction over the next two years. Residential construction will not fundamentally bottom until the middle of summer as a result of the lags associated with housing starts. Moreover, a slight increase in the mix toward apartment units will prevent any significant liftoff of residential construction. Nevertheless, construction probably will reach a low point in August and begin a gradual improvement thereafter.

Declining site prices and constraints on wages has continued to restrict the growth in the construction deflator. As housing improves, however, site values may rise. In addition, wage concessions given by construction employees should diminish. Nevertheless, no significant acceleration is expected in the construction deflator.

Business Activity - Durable goods activity was stronger than anticipated as non-electrical machinery and primary metals rebounded to their February levels. Apparently, their dips in March were aberrations. Aircraft orders remain strong but were not significant contributors to growth. Defense orders actually declined following a one-month surge. Although more aircraft orders could push durable goods orders to new highs in the next month or so, some slowing is anticipated in orders for primary metals while transportation equipment other than aircraft should decline as auto sales incentives diminish. Thus, durable goods orders probably are peaking at the present time and should gradually diminish.

Nevertheless, the substantial backlogs that currently exist suggest a significant increase in capital shipments over the next year. According to the latest plant and equipment surveys, expenditures are expected to be up 6.5% after adjustment for inflation. Assuming slightly more than 3% for capital equipment prices, this means that shipments should grow just under double-digit levels. These estimates are broadly consistent with the shipments projections presented here.

Some of the sharp rebound in business inventories reflects higher prices for energy materials. Excluding those factors and the goods in process, business inventories actually are growing slowly. A rebound in inventories is anticipated, however, as sales activity picks up during the summer.

The rebound in industrial activity during April suggests that not all the employment gains were statistical flukes for that month. However, activity should decline in May with industrial materials showing significant weakness.

Prices - Composition factors have been significant in restraining price increases for consumer durables. However, increases in auto sales relative to other durables activities should lead to some acceleration in the consumer durables deflator during the summer months. Prices are currently growing sharply for consumer non-durables but are expected to slow early next year. Although rental rates should intensify in consumer services, transportation services probably will show slower price increases than previously anticipated. Moreover, reduced liability fees should moderate medical pricing. As a result, the service price deflator is not expected to grow quite as rapidly as originally anticipated. This should result in a slightly more moderate increase in the consumption deflator and in the CPI than originally anticipated.

Miscellaneous - After higher oil prices finally are reflected in the merchandise trade balance, the strong dollar should aid the J effect for several more months. Indeed, the trade balances could be coming down again in the summer. However, the strong dollar probably will impact trade activity late this year and early next year. This, in turn, should lead to reductions in currency values. The dollar probably is nearing a peak, although further declines in interest rates probably would be necessary before that assumption could be firmly held.

The April rise in the leading indicators came after two monthly declines. However, enough information already is known to indicate that the indicators will be down in May. If orders fall significantly, the indicators could decline sharply. Weakness is coming from the workweek, sensitive prices, initial claims, and the inflation-adjusted money stock. Only the stock market is providing substantial strength at the present time.

Corporate profits were even weaker than anticipated during the first quarter. As a result, adjusted profits are lower than anticipated. A rebound is expected in profits during the summer as the IVA declines significantly from current levels. In addition, the decline in interest rates should reduce the interest recipient's share of capital's earnings. This allows for more equity growth. When these improved profit conditions are combined with anticipated declines in yields on government bonds, equity values perform nicely. Indeed, assuming that current values are appropriately reflecting current earnings and interest rate conditions, equity markets could go higher over the next year. However, the road should be bumpy with significant dips in the fall before new highs are generated early next year. Then, potential recessionary behavior again will reduce equity values.

Financial Markets

As mentioned in previous projections, sharp increases in household savings and temporary improvements in government deficits should have been sufficient to offset increased borrowing needs by the corporate sector. The only factor apparently preventing interest rates from declining was the reluctant foreign investor. When that foreign investor changed directions early this year, interest rates were set to decline. However, Federal Reserve restraint prevented short rates from adjusting. Therefore, all of the significant adjustment had to occur on the long side of the market.

The Federal Reserve remains reluctant to adjust interest rates downward. Commercial paper rates at the present time are leading the short rates down. As long as the Federal Reserve persists in lagging behind other short-term rates, long-term interest rates should continue trending downward. Of course, as the economy slows further, the Federal Reserve eventually will relent, allowing a significant drop in the federal funds rate. This will ultimately lead to a significant decline in the prime rate. However, some plateau in interest rates should develop in the summer or late fall when inventories again are rebuilt. At that time, government borrowings will be intensifying while household savings rates probably will be dipping slightly. On balance, however, interest rates are trending downward. Indeed, declining short-term interest rates should be expected, causing further declines in long-term rates, until the federal funds rate catches up with the commercial paper rate. A strong buy signal for long-term securities should have been read when the commercial paper rates fell 20 basis points below the federal funds rates. As long as commercial paper rates remain significantly below the federal funds rate, the bond market rally will persist.

Equity Markets - Although loan demand must remain a cause of some concern, declining interest rates are almost always beneficial to financial institutions. In addition, the credit-sensitive securities, including home builders, should begin performing well. Foreigners will continue to buy the Dow and other big name stocks, but their flows into the financial markets should not persist too much longer. Therefore, the equity markets should begin rotating toward the second tier in high-growth stocks. Thus, financial institutions, interest-sensitive securities, and some technology considerations in the secondary market all could do well. Although our current formulas suggest that any stock market correction will be modest and could be delayed until the fall, my own inclination is to anticipate a more significant correction sooner than that. In any event, barring a significant forecasting error, equity values remain reasonable for long-term investors.

Until the dollar begins relenting, multi-national corporations should be avoided. In addition, the foreign investors probably are overpricing the Dow-based securities. This suggests that a rotation in the stock market should begin with small gains in the overall averages but significant potential for the less known issues.

EMPLOYMENT

	Payroll Employment		Index of Hours Worked		Household Civilian Employment		Civilian Unemployment Rate		Hourly Earnings	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	108065	107442	128.3	127.4	116711	116711	5.4	5.4	9.49	9.49
February	108341	107711	127.8	127.2	116853	116853	5.1	5.1	9.50	9.52
March	108512	107888	128.1	127.6	117136	117136	5.0	5.0	9.52	9.54
April	108695	108094	129.5	128.7	117226	117113	5.2	5.3	9.58	9.60
May	108820	108195	128.0	127.5	117363	117215	5.2	5.2	9.62	9.61
June	108946	108358*	128.5	127.9*	117502	117380*	5.1	5.3*	9.66	9.65*
July	109167	108690	128.9	128.2	117743	117695	5.1	5.2	9.70	9.69
August	109384	108906	129.3	128.4	117979	117907	5.0	5.2	9.74	9.72
September	109602	109207	129.7	128.7	118208	118203	5.0	5.1	9.78	9.76
October	109715	109508	129.5	129.0	118328	118502	5.0	5.0	9.82	9.80
November	109832	109800	129.7	129.3	118497	118803	5.1	5.0	9.86	9.83
December	109950	110025	129.9	129.5	118654	119068	5.0	5.0	9.90	9.86
January 1990	110106	110346	130.0	129.8	118827	119367	5.0	4.9	9.94	9.90
February	110303	110544	130.2	130.0	119012	119606	5.0	4.9	9.98	9.94
March	110501	110638	130.3	130.0	119296	119683	5.1	5.0	10.02	9.98
April	110605	110543	130.4	129.8	119337	119635	5.1	5.2	10.06	10.02
May	110636	110534	130.4	129.8	119305	119658	5.2	5.3	10.10	10.06
June	110640	110392	130.3	129.6	119324	119519	5.3	5.5	10.14	10.10

PERSONAL INCOME

	Personal Income		Wage & Salary		Personal Savings		Disposable Income		Personal Outlays	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	4.272	4.272	2.559	2.559	187.9	190.6	3.659	3.659	3.472	3.469
February	4.316	4.317	2.571	2.571	213.7	218.1	3.701	3.701	3.487	3.482
March	4.350	4.352	2.592	2.592	234.0	234.8	3.729	3.728	3.495	3.494
April	4.378	4.369	2.607	2.608	220.8	198.7	3.750	3.729	3.529	3.530
May	4.398	4.387*	2.619	2.605*	207.9	210.8*	3.765	3.762*	3.557	3.551*
June	4.420	4.405	2.631	2.625	206.2	211.9	3.781	3.776	3.575	3.564
July	4.450	4.431	2.649	2.644	214.2	215.1	3.814	3.798	3.600	3.583
August	4.481	4.452	2.667	2.657	211.5	206.7	3.834	3.815	3.623	3.608
September	4.511	4.481	2.685	2.676	218.0	214.9	3.855	3.840	3.637	3.625
October	4.534	4.509	2.699	2.694	219.3	218.3	3.875	3.864	3.656	3.646
November	4.554	4.533	2.709	2.709	221.5	218.0	3.894	3.884	3.673	3.666
December	4.573	4.557	2.719	2.723	226.3	218.7	3.916	3.905	3.690	3.686
January 1990	4.600	4.582	2.738	2.742	227.4	217.9	3.938	3.927	3.711	3.709
February	4.626	4.606	2.759	2.758	227.4	218.2	3.960	3.947	3.733	3.729
March	4.652	4.628	2.780	2.771	227.0	216.2	3.982	3.965	3.755	3.749
April	4.669	4.646	2.791	2.779	223.4	212.9	3.995	3.979	3.772	3.766
May	4.685	4.669	2.801	2.792	216.0	214.2	4.009	3.998	3.793	3.784
June	4.701	4.686	2.810	2.800	214.0	204.9	4.026	4.011	3.812	3.806

Fore. = May Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

CONSUMPTION

	Personal Consumption		Durables		Nondurables		Services		Consumption Real	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	3367.8	3364.9	469.1	467.2	1088.9	1088.9	1809.8	1808.8	2634.1	2632.5
February	3383.2	3378.1	461.0	458.5	1093.9	1091.9	1828.4	1827.7	2641.0	2638.8
March	3390.3	3388.6	454.3	452.6	1098.4	1098.2	1837.6	1837.7	2629.4	2629.4
April	3424.2	3424.5	463.7	467.1	1110.3	1105.4	1850.2	1852.1	2642.1	2638.0
May	3451.8	3445.0*	468.5	464.4*	1121.2	1115.0*	1862.1	1865.6*	2651.1	2639.9*
June	3469.2	3457.3	467.6	458.5	1127.6	1122.5	1874.0	1876.3	2652.3	2636.9
July	3493.8	3475.5	470.3	457.5	1134.3	1128.9	1889.2	1889.1	2660.9	2641.0
August	3516.1	3500.3	473.9	464.7	1138.6	1134.2	1903.6	1901.4	2669.8	2651.7
September	3530.2	3516.6	469.4	463.8	1142.8	1137.5	1918.0	1915.3	2672.4	2654.7
October	3548.4	3536.7	470.6	465.2	1147.3	1143.7	1930.5	1927.8	2674.0	2661.1
November	3564.8	3556.4	469.0	467.7	1152.8	1148.1	1943.0	1940.6	2674.3	2668.0
December	3581.5	3576.1	467.7	469.3	1158.2	1153.3	1955.6	1953.5	2674.8	2672.9
January 1990	3602.4	3598.4	469.9	472.6	1163.6	1159.1	1968.9	1966.7	2680.4	2679.9
February	3624.0	3617.6	472.1	473.0	1169.7	1164.3	1982.2	1980.3	2688.4	2684.8
March	3645.6	3637.1	474.3	472.4	1175.8	1171.3	1995.5	1993.4	2694.5	2689.6
April	3662.2	3653.9	472.7	470.9	1180.2	1176.8	2009.3	2006.2	2694.8	2691.4
May	3683.2	3671.2	475.1	470.2	1183.5	1181.5	2024.6	2019.5	2696.3	2692.9
June	3701.7	3693.1	475.1	473.0	1186.7	1186.4	2039.9	2033.7	2698.0	2698.4

RETAIL SALES

	Retail Sales		Non-Auto Durables		Auto (Million Units)		Nondurable Sales		Auto Sales	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	140.04	140.04	22.62	22.62	9.8	9.8	86.23	86.23	31.19	31.19
February	139.43	139.43	22.43	22.43	9.9	9.9	86.36	86.36	30.64	30.64
March	139.36	139.36	22.13	22.13	9.6	9.6	86.76	86.76	30.48	30.48
April	139.93	139.93	21.83	21.83	10.8	10.8	87.30	87.30	30.81	30.81
May	141.36	141.02*	22.34	22.06*	10.0	10.5*	88.16	88.16*	30.86	30.80*
June	141.74	140.93	22.54	22.15	9.6	10.0	88.66	88.75	30.54	30.03
July	142.58	141.33	22.47	22.06	9.8	9.9	89.19	89.26	30.92	30.01
August	143.33	142.57	21.95	21.95	10.5	10.4	89.53	89.68	31.85	30.94
September	143.15	142.73	21.87	21.92	10.2	10.3	89.86	89.94	31.42	30.82
October	143.63	143.37	22.17	21.98	9.8	10.0	90.21	90.43	31.25	30.96
November	143.88	144.01	22.02	22.07	9.7	10.1	90.64	90.78	31.22	31.16
December	144.16	144.60	21.46	22.03	9.9	10.2	91.07	91.19	31.63	31.38
January 1990	144.83	145.44	21.60	22.20	9.9	10.3	91.49	91.65	31.74	31.59
February	145.56	145.89	21.64	22.16	10.0	10.3	91.97	92.06	31.95	31.67
March	146.29	146.37	21.96	22.21	9.9	10.2	92.45	92.61	31.88	31.55
April	146.46	146.64	21.90	22.23	9.8	10.1	92.80	93.05	31.76	31.36
May	146.99	146.94	21.88	22.27	10.0	10.0	93.06	93.42	32.05	31.25
June	147.24	147.64	21.70	22.35	10.1	10.1	93.31	93.81	32.23	31.48

Fore. = May Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

CONSTRUCTION

	Housing Starts		Single Family Starts		Housing Permits		Construction Expenditures (Current)		Construction Expenditures (Real)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	1.678	1.678	1.199	1.199	1.486	1.486	418.0	418.0	358.9	358.9
February	1.465	1.465	1.029	1.029	1.403	1.403	414.8	415.7	355.7	356.6
March	1.399	1.399	0.986	0.986	1.230	1.230	413.5	414.6	354.2	355.2
April	1.361	1.361	1.015	1.036	1.318	1.318	409.3	414.9	350.1	355.3
May	1.406	1.393*	1.021	1.026*	1.305	1.305*	409.0	413.6*	349.6	353.5*
June	1.412	1.407	0.970	1.025	1.317	1.311	409.2	412.0	349.1	351.5
July	1.354	1.402	0.968	1.028	1.267	1.301	408.3	410.4	347.2	349.6
August	1.342	1.417	0.963	1.046	1.246	1.314	407.2	409.4	345.7	348.4
September	1.327	1.427	0.958	1.051	1.229	1.326	406.0	410.6	344.1	348.6
October	1.335	1.437	0.952	1.043	1.238	1.338	408.6	410.2	345.7	347.6
November	1.340	1.418	0.947	1.026	1.245	1.325	410.8	410.3	347.0	347.1
December	1.343	1.434	0.943	1.035	1.249	1.339	412.9	411.8	348.1	347.8
January 1990	1.296	1.450	0.935	1.039	1.217	1.358	413.0	411.8	347.6	346.9
February	1.304	1.460	0.928	1.048	1.223	1.369	414.1	414.2	348.0	348.4
March	1.321	1.470	0.921	1.059	1.229	1.382	414.1	415.1	347.1	348.5
April	1.327	1.474	0.935	1.068	1.234	1.380	416.0	416.2	348.1	348.9
May	1.335	1.504	0.942	1.082	1.236	1.403	417.7	417.8	348.7	349.6
June	1.343	1.486	0.949	1.075	1.245	1.379	419.5	419.7	349.6	350.6

	Non-Residential		Public Construction		Residential Construction	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	135.1	135.1	81.4	81.4	201.4	201.4
February	133.7	134.1	81.5	82.0	199.6	199.7
March	138.7	138.5	74.1	75.0	200.7	201.1
April	136.6	134.9	76.5	79.3	196.2	200.7
May	136.4	135.4*	76.9	79.0*	195.7	199.2*
June	136.6	135.0	77.3	79.5	195.3	197.5
July	137.0	134.3	77.9	78.8	193.4	197.3
August	137.4	134.0	78.4	79.3	191.4	196.1
September	137.7	133.6	78.8	79.4	189.5	197.6
October	138.5	133.1	79.5	80.1	190.6	197.0
November	139.3	133.4	80.0	80.0	191.5	196.9
December	140.0	133.2	80.5	80.6	192.4	198.0
January 1990	140.3	134.7	80.9	80.5	191.8	196.6
February	140.7	135.3	81.4	81.1	192.0	197.8
March	141.1	136.0	80.8	80.9	192.2	198.2
April	141.5	136.4	81.2	81.2	193.3	198.6
May	141.3	136.9	81.8	81.6	194.6	199.3
June	141.3	137.2	82.3	82.1	195.9	200.4

Fore. = May Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

BUSINESS ACTIVITY

	Manufacturers' Inventories		Durable Goods Orders		Non-Defense Capital Goods Orders		Non-Defense Capital Shipments	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	357.5	357.5	128.48	128.48	40.35	40.35	33.33	33.33
February	359.1	359.1	124.11	124.11	37.19	37.19	33.46	33.46
March	360.4	361.1	125.21	125.38	38.09	38.14	34.03	34.08
April	363.4	363.3	126.63	129.16	37.76	40.48	34.26	34.48
May	365.3	365.1*	126.94	128.77*	37.85	39.22*	34.39	34.63*
June	367.2	367.3	126.27	127.65	37.12	39.03	34.52	34.92
July	370.5	369.9	126.43	127.93	36.69	39.12	34.82	35.26
August	373.4	372.5	126.68	128.46	36.63	38.83	35.03	35.43
September	376.2	375.0	126.29	128.21	36.17	38.75	35.24	35.81
October	378.9	377.4	125.76	127.92	35.84	38.61	35.36	35.96
November	381.1	380.1	125.43	127.95	35.53	38.69	35.45	36.05
December	383.3	382.8	125.89	128.16	35.72	38.84	35.75	36.29
January 1990	385.2	384.5	126.14	127.43	35.88	38.06	35.66	36.15
February	387.4	386.3	126.35	127.02	36.17	37.43	35.87	36.52
March	389.6	388.2	126.12	127.28	35.93	37.56	36.02	36.69
April	390.9	390.8	125.56	126.93	35.76	37.06	36.05	36.60
May	391.3	391.3	124.85	126.56	35.49	36.84	36.01	36.29
June	391.7	393.1	125.18	126.84	35.64	37.05	35.99	36.43

	Business Inventories		Defense Shipments		Industrial Production		Capacity Utilization	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	759.8	759.8	8.73	8.73	140.8	140.8	84.3	84.3
February	763.6	763.1	8.40	8.40	140.4	140.4	83.9	83.9
March	765.6	765.6	8.50	8.45	140.5	140.5	83.7	83.7
April	772.3	769.5*	8.58	8.65	140.9	141.1	83.8	83.9
May	779.6	775.6	8.62	8.73*	141.2	140.9*	83.9	83.6*
June	786.8	781.9	8.62	8.70	141.5	141.2	84.0	83.7
July	789.9	787.3	8.55	8.75	142.7	141.5	84.4	83.7
August	793.0	793.2	8.61	8.77	143.9	141.7	84.8	83.6
September	795.9	797.4	8.67	8.82	145.1	142.0	85.2	83.6
October	801.4	800.6	8.62	8.76	144.7	142.3	84.7	83.6
November	808.9	804.3	8.70	8.75	144.3	142.6	84.3	83.7
December	816.3	808.9	8.78	8.81	144.6	142.8	84.4	83.7
January 1990	819.4	815.3	8.68	8.84	144.5	143.1	84.1	83.7
February	822.0	819.4	8.76	8.87	144.2	143.3	83.8	83.7
March	824.6	823.6	8.90	8.93	143.9	143.3	83.5	83.5
April	828.5	827.5	8.74	8.90	143.4	143.0	83.1	83.2
May	832.4	830.4	8.67	8.95	142.9	142.8	82.7	82.9
June	836.3	834.5	8.60	8.97	142.5	142.5	82.4	82.5

Fore. = May Forecast
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* = This item and those beyond it are expectations.

PRICES

	CPI-U (seasonally adjusted)		PPI Finished Goods (seasonally adjusted)		PPI-Industrial Commodities (unadjusted)		Estimated GNP Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	121.4	121.4	111.0	111.0	109.1	109.1	125.0	125.0
February	121.9	121.9	112.1	112.1	110.0	110.0	125.2	125.2
March	122.5	122.5	112.6	112.6	110.6	110.6	125.5	125.5
April	123.4	123.1	113.1	113.3	111.3	111.3	126.1	126.3
May	124.1	123.8	113.8	114.0	112.0	111.7	126.8	127.0
June	124.5	124.4*	114.2	114.3*	112.7	112.2	127.2	127.5
July	125.1	124.9	114.4	114.6	113.0	112.8	127.5	128.0
August	125.6	125.3	114.7	114.9	113.5	113.3	127.9	128.3
September	126.2	125.8	114.7	115.0	112.5	112.1	128.3	128.8
October	126.7	126.2	115.0	115.4	113.9	113.7	128.8	129.2
November	127.2	126.6	115.3	115.7	114.0	114.0	129.3	129.6
December	127.8	127.1	115.6	116.0	114.2	114.3	129.2	130.0
January 1990	128.2	127.6	116.0	116.3	114.8	114.8	130.4	130.5
February	128.5	128.0	116.5	116.6	115.6	115.2	131.0	130.9
March	128.9	128.5	116.8	117.0	116.4	115.7	131.6	131.3
April	129.5	129.1	117.2	117.3	116.8	116.2	132.1	131.8
May	130.2	129.6	117.6	117.7	117.1	116.7	132.7	132.3
June	130.9	130.2	118.1	118.1	117.4	117.1	133.3	132.8

	Consumption Deflator		Consumer Durables		Consumer Nondurables		Consumer Services		Implicit Construction Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	127.9	127.8	112.0	112.0	119.4	119.4	138.9	138.8	116.4	116.4
February	128.1	128.0	111.7	111.5	119.5	119.5	139.2	139.1	116.6	116.6
March	128.9	128.9	111.3	111.1	121.0	121.0	139.9	139.9	116.7	116.7
April	129.6	129.8	111.6	111.5	122.2	122.8	140.5	140.4	116.9	116.8
May	130.2	130.5*	111.8	111.5*	123.2	123.6	141.1	141.2	117.1	117.0
June	130.8	131.1	112.0	111.8	123.6	124.1	141.7	141.9	117.3	117.2
July	131.3	131.6	112.4	112.1	123.8	124.4	142.3	142.5	117.6	117.4
August	131.7	132.0	112.7	112.4	124.0	124.7	142.9	143.1	117.8	117.5
September	132.1	132.5	113.0	112.6	124.2	125.0	143.5	143.7	118.0	117.8
October	132.7	132.9	113.2	112.8	124.8	125.3	144.2	144.3	118.2	118.0
November	133.3	133.3	113.4	113.0	125.3	125.5	144.9	144.9	118.4	118.2
December	133.9	133.8	113.4	113.3	125.9	125.9	145.6	145.5	118.6	118.4
January 1990	134.4	134.3	113.7	113.6	126.3	126.3	146.2	146.1	118.8	118.7
February	134.8	134.7	114.0	113.9	126.6	126.6	146.9	146.7	119.0	118.9
March	135.3	135.2	114.3	114.1	127.0	127.0	147.5	147.3	119.3	119.1
April	135.9	135.8	114.4	114.3	127.7	127.5	148.3	147.9	119.5	119.3
May	136.6	136.3	114.5	114.5	128.4	128.1	149.0	148.5	119.8	119.5
June	137.2	136.9	114.4	114.6	129.0	128.6	149.7	149.2	120.0	119.7

Fore. = May Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

MISCELLANEOUS

	Merchandise Trade Balance		Leading Indicators	Estimated GNP		Estimated GNP (1982 $)		IVA (annual rate)	
	Fore.	C.E.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	-8.68	-8.68	145.9	5109	5101	4087	4087	-26.7	-26.7
February	-9.82	-9.82	145.4	5114	5103	4085	4076	-39.6	-39.6
March	-8.86	-8.86	144.6	5127	5111	4085	4073	-41.7	-42.2
April	-9.73	-9.78*	145.7	5163	5156	4094	4082	-40.2	-45.3
May	-9.92	-10.04	144.8*	5197	5183	4099	4081	-28.6	-38.4
June	-9.42	-9.93	145.1	5231	5218	4112	4093	-23.5	-31.3
July	-10.21	-9.65	144.5	5256	5243	4122	4096	-25.5	-28.4
August	-10.88	-9.36	144.2	5288	5275	4134	4111	-28.0	-23.2
September	-10.83	-9.07	144.0	5320	5301	4147	4116	-29.9	-23.1
October	-10.62	-9.26	143.2	5341	5328	4147	4124	-28.6	-16.9
November	-10.25	-9.55	143.5	5359	5352	4145	4130	-27.4	-17.3
December	-9.56	-9.67	143.6	5379	5375	4147	4135	-26.3	-17.4
January 1990	-9.93	-10.01	142.9	5405	5401	4145	4139	-30.2	-19.4
February	-10.58	-10.25	142.6	5442	5428	4154	4147	-32.4	-21.8
March	-10.86	-10.43	143.1	5480	5450	4164	4151	-34.6	-24.3
April	-9.85	-10.26	143.0	5493	5473	4158	4153	-31.1	-25.6
May	-9.52	-10.42	143.2	5502	5494	4146	4153	-29.9	-26.1
June	-9.37	-10.53	143.0	5508	5515	4132	4153	-28.7	-26.0

	Currency Index		Adjusted Profits		30-Year Government Bonds		New York Composite	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	95.12	95.12	210.5	193.6	8.93	8.93	160.40	160.40
February	95.77	95.77	163.4	163.9	9.01	9.01	165.08	165.08
March	96.99	96.99	156.5	155.5	9.17	9.17	164.60	164.60
April	97.23	97.24	165.9	159.8	9.32	9.03	165.13	170.34
May	97.95	100.81	178.2	154.7	9.40	8.78*	166.29	175.56
June	98.56	100.93*	180.3	169.2	9.36	8.37	164.21	182.26*
July	97.43	98.85	177.4	173.3	9.30	8.49	156.82	184.04
August	95.82	98.21	175.7	184.1	9.25	8.43	153.54	186.90
September	94.16	95.43	174.0	186.3	9.21	8.27	150.26	183.11
October	93.09	95.62	173.1	189.2	9.18	8.46	148.29	181.78
November	91.70	96.43	172.4	191.4	9.12	8.59	148.86	181.12
December	90.36	96.81	171.9	193.7	9.15	8.50	149.30	185.23
January 1990	91.25	95.01	169.8	192.5	9.06	8.36	145.14	187.17
February	94.46	93.28	169.1	194.8	9.01	8.27	140.53	191.46
March	94.05	92.29	168.2	195.2	8.92	8.16	138.27	194.44
April	91.02	90.85	168.5	191.6	8.78	8.09	139.45	192.51
May	89.63	91.65	166.1	186.2	8.73	8.05	140.25	188.01
June	88.26	93.46	163.7	181.4	8.70	7.98	141.06	184.77

Fore. = May Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

FINANCIAL MARKETS

	Monetary Base		M1		M2		Federal Funds		T-Bills (6 Mos.)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	287.9	287.9	786.3	786.3	3065.9	3065.6	9.12	9.12	8.36	8.36
February	287.5	287.5	787.4	787.4	3069.7	3069.7	9.36	9.36	8.55	8.55
March	289.4	289.3	786.3	786.3	3079.5	3079.5	9.85	9.85	8.85	8.85
April	290.3	289.0	782.9	782.9	3090.4	3081.1	9.84	9.84	8.65	8.65
May	292.9	289.8*	785.3	774.4*	3101.3	3071.7*	9.83	9.77*	8.74	8.33*
June	295.5	291.1	787.2	777.2	3112.2	3086.8	9.83	9.53	8.83	8.16
July	297.3	293.2	792.5	783.7	3134.6	3105.6	10.20	9.50	8.89	8.09
August	298.1	294.7	798.9	789.2	3158.6	3122.3	10.23	9.26	8.86	7.94
September	298.9	296.5	804.9	794.9	3182.5	3140.9	10.26	9.21	8.83	7.96
October	300.4	298.2	808.6	800.1	3195.6	3157.4	10.32	9.26	8.81	7.92
November	302.8	300.0	812.4	805.2	3213.2	3177.5	10.29	9.30	8.82	7.99
December	305.2	301.7	816.2	810.1	3231.0	3196.8	10.26	9.33	8.80	8.03
January 1990	306.9	303.4	821.7	815.5	3250.4	3214.1	10.01	9.27	8.73	7.94
February	307.8	305.1	828.6	820.4	3270.3	3233.4	9.96	9.23	8.62	7.91
March	308.7	306.8	835.4	825.9	3290.1	3255.1	9.84	9.15	8.51	7.78
April	310.5	308.2	840.3	829.1	3314.3	3273.7	9.56	8.86	8.47	7.61
May	312.5	309.7	845.0	833.1	3326.1	3289.5	9.55	8.75	8.41	7.52
June	314.4	311.3	849.8	836.8	3338.0	3306.1	9.56	8.62	8.36	7.40

	Aaa (Seasoned)		Municipals (Bond Buyer)		(3 Month) Commercial Paper		90 Day CD's		Prime Rate	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	9.62	9.62	7.35	7.35	9.04	9.04	9.20	9.20	10.50	10.50
February	9.64	9.64	7.44	7.44	9.37	9.37	9.51	9.51	10.93	10.93
March	9.80	9.80	7.59	7.59	9.95	9.95	10.09	10.09	11.50	11.50
April	9.79	9.79	7.49	7.49	9.81	9.81	9.94	9.94	11.50	11.50*
May	9.75	9.54*	7.45	7.22*	9.80	9.56*	9.93	9.68*	11.50	11.50
June	9.83	9.32	7.51	6.94	9.86	9.34	9.97	9.47	11.50	11.14
July	9.89	9.17	7.58	6.73	10.17	9.30	10.26	9.41	11.68	11.00
August	9.95	9.05	7.64	6.71	10.26	9.16	10.35	9.29	12.00	10.83
September	9.99	9.11	7.68	6.75	10.23	9.20	10.30	9.30	12.00	10.50
October	9.90	9.20	7.62	6.83	10.30	9.14	10.41	9.24	12.00	10.50
November	9.83	9.27	7.53	6.89	10.25	9.18	10.37	9.31	12.00	10.50
December	9.76	9.25	7.47	6.90	10.22	9.25	10.33	9.38	12.00	10.50
January 1990	9.70	9.22	7.40	6.87	10.07	9.21	10.22	9.34	12.00	10.50
February	9.67	9.07	7.38	6.73	9.98	9.14	10.09	9.16	11.96	10.50
March	9.64	8.98	7.35	6.65	9.88	9.05	10.05	9.08	11.50	10.50
April	9.56	8.86	7.26	6.54	9.59	8.74	9.76	8.87	11.50	10.50
May	9.53	8.73	7.20	6.49	9.53	8.69	9.71	8.81	11.28	10.42
June	9.50	8.66	7.18	6.38	9.50	8.56	9.65	8.69	11.00	10.00

Fore. = May Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

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ECONOMIC FORECASTING CENTER

MONTHLY PROJECTIONS
June 1989

Dr. Donald Ratajczak, Director
For Release: Wednesday, July 19, 1989

HAS THE RECESSION'S FIRST CHAPTER BEEN WRITTEN?

Although the employment report for June showed some weakness, especially in the goods-producing sector, enough jobs appear to have been generated in the service sector to eliminate any question that the United States currently is in recession. Certainly, the diffusion index, which showed that 54% of more than 340 industries reported employment gains, is sufficient to eliminate any recessionary questions. However, a separate diffusion index for manufacturing showed only 46% recording employment gains. This is consistent with a call of recession in the industrial sector. Moreover, that decline was the third consecutive performance of less than 50% employment gains.

Industrial weakness surfaced as well in the industrial production report for June. Not only was activity down by 0.2%, but the May figure was revised to a modest decline. Significantly, activity declined for business equipment as well as for consumer goods. Damp and cool weather and a coal miners' strike also impacted the June index. Also, retail activity showed weakness, with sales falling 0.4% in June following a 0.1% decline in May. Weakness in auto sales accounted for the slowdown, but sales adjusted for inflation clearly are also down from January levels.

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Indeed, the weakness in industrial activity appears to be the result of production plans that have exceeded actual sales. Instead of adjusting inventories downward, the latest manufacturing report showed a significant increase in inventories. Moreover, inventories of finished goods increased 1%. They were up even more for nondurables. When these facts are coordinated with the report by purchasing managers that orders weakened in June and that employment moderated, further declines in production may develop. Certainly, shipments exceeded orders by a very meager margin in May.

Even the inflationary indices are showing signs of weakness. Although the producer price index for finished goods increased 0.7% excluding food and energy in June, the index less food and energy at the intermediate and crude materials levels both fell sharply. Sensitive prices measured by the Journal of Commerce index peaked in April, although they have not declined dramatically from those peak levels.

Of course, the creation of more than 150,000 service jobs does not reflect a recession. At the same time, those service jobs were heavily concentrated in health services and miscellaneous services. The latter sector can be revised significantly in subsequent reports. Employment in the trade sector was flat in June and only rose modestly in the transportation and financial services areas. Thus, the economy is not experiencing robust growth at the present time.

To further accentuate the developing weakness, seasonally-adjusted commercial and industrial loans at commercial banks fell significantly in the latter half of June. This reverses strong increases in the past two months. Short-term interest rates continued to ease, with rates for commercial paper continuing to fall more than 0.3 percentage points below the federal funds rate. Indeed, short-term interest rates would fall further except for the very gradual downward movement of interest rate targets by the Federal Reserve.

In short, weakness in retail activity, rising orders for finished goods, declines in industrial production, weakness in productivity, and softness for short-term interest rates all are consistent with the first chapter of an economic recession. Thus, the prospects that a recession could be about to begin cannot be totally dispelled. On the other hand, recessions do not start when employment gains continue to exceed 150,000 per month. Even though initial claims have risen recently, recessionary claims usually are in the 450,000 - 550,000 weekly range. This is well above the 340,000 that have been recorded in recent weeks. For those reasons, a recession certainly has not yet begun. However, the first chapter of the next recession will read like the indicators that were released last Friday.

Quarterly Profile of GNP

	1989-1	1989-2	1989-3	1989-4	1990-1	1990-2	1989 Annual	1990 Annual
Real:	4.4	0.5	2.0	2.1	1.4	0.2	2.5	1.0
Price:	3.6	5.1	4.0	4.3	4.6	4.8	4.6	4.5
Nominal:	8.2	5.7	6.1	6.5	6.1	5.1	7.2	5.6

Monthly Statistical Highlights

	June 1989	July 1989	Aug 1989
Payroll Employment		+165,000	+176,000
Index of Hours Worked		+0.2%	+0.2%
Household Employment		+172,000	+192,000
Civilian Unemployment Rate		5.3%	5.3%
Personal Income	+0.4%	+0.4%	+0.5%
Savings Rate	5.3%	5.3%	5.1%
Personal Consumption	+0.5%	+0.4%	+0.7%
Retail Sales		-0.1%	+0.7%
Auto Sales		9.9*	10.2*
Housing Starts	+2.2%	+2.3%	-0.2%
Housing Permits	-2.2%	+0.4%	-0.6%
Construction Expenditures	-1.3%	+0.9%	+0.9%
Business Inventories	+0.6%	+0.6%	+0.6%
Orders for Durable Goods	-0.8%	+1.4%	-1.3%
Orders - Nondefense Capital Goods	-0.5%	+1.3%	-3.4%
Industrial Production		-0.1%	UNC
CPI		+0.3%	+0.3%
PPI		+0.1%	+0.2%
Consumption Deflator	+0.3%	+0.3%	+0.3%
Leading Indicators	-0.2%	+0.4%	-0.2%
Currency Index		-3.2%	-2.5%
Equity Index		+4.3%	+1.3%
Real GNP (annual rate)	+2.1%	+1.2%	+4.5%
M1 (annual rate)		+5.3%	+8.7%
M2 (annual rate)		+7.4%	+8.7%

* auto sales in millions

COMMENTARY

EMPLOYMENT - For the third consecutive month, more manufacturing industries reduced employment than increased it. However, sharp increases in service employment led to a 180,000 increase in payrolls. In addition, the May increase was revised upward from 101,000 to 207,000. However, the workweek declined to the lowest level in more than six years. Employment gains were sufficient to allow a modest increase in the index of hours worked. However, heavy rain led to a reduction in hours worked in construction while manufacturing hours also declined. A sharp increase in the unemployment of teenagers led to a slight increase in overall unemployment rates. This could be the result of seasonal employment factors in June. If so, the unemployment rate would be susceptible to a decline in July. However, further weakness is expected in employment opportunities. Employment also was flat for retail trade and showed only modest gains in the finance and transportation sectors.

For the second consecutive month, hourly earnings showed little growth. Of course, layoffs in the manufacturing sector were in the high-wage areas, that could be depressing that series. Nevertheless, hourly earnings are only up 3.8% from a year ago and they are showing no significant trend at the present time. Shrinkage in the workweek possibly could mean more significant layoffs next month.

PERSONAL INCOME AND OUTLAYS - A substantial upward revision in tax collections led to significant declines in disposable income and personal savings in the past few months. As a result, the savings rate now is only 5.3% rather than more than 6%. Of course, the result of this is improved federal revenues leading to lower deficits than previously expected. Weak gains in wages and salaries indicated that the declining workweek was largely correct for May. Some rebound is expected in wage and salary income in June, but there should be a slowing in gains from interest income. As interest earnings grow more slowly, gains in personal income also will be reduced.

Farm income also has weakened as subsidies have diminished. Further weakness is expected in the next few months before a rebound should develop at the time of the September harvest.

Sharp increases in financial and utility services led to a significant increase in consumer spending during May. Excluding that surge, consumer spending would have declined. Cloudy weather should hold down utility spending in June although financial services remained strong. Auto sales weakened but some modest rebound is expected in sales of nondurable goods.

In June, retail sales fell 0.4% as a result of a dip in auto sales. This is consistent with the reduction in unit sales. However, auto sales are picking up slightly early in July. Thus, some rebound in retail sales should be expected that month. Nevertheless, weakening prices for food and energy will be reflected in continued flatness in sales of nondurable goods.

CONSTRUCTION - As expected, single-family housing sales fell in May reflecting lower permits during the previous month. As some strength has developed in those permits, a slight rebound could be anticipated in June starts. However, most of the strength currently is anticipated in apartment construction, which reached unusually low levels early in spring.

A revision of construction expenditures led to substantially higher spending on public construction than originally reported. Some upward revisions also were reported for residential activity. In addition, the sharp rebound in public construction during May was contained in conservation and miscellaneous public projects. These gains are not expected to persist. On the other hand, nonresidential private construction remains sluggish. Further moderate weakness is anticipated in June before a modest rebound should develop later in the year. Industrial construction has leveled while commercial construction other than office buildings has weakened considerably. This generally reflects retail space activity. Further weakness is anticipated in retail construction through the summer months.

The revision also raised the implicit costs of construction goods. As a result, the GNP deflator probably will be revised upward for the past year or so.

Damp weather probably will continue to restrain construction expenditures in the early summer months before a rebound is anticipated. However, weakness in nonresidential construction and no further growth in public construction should lead to further moderate weakness in construction despite a rebound in housing activity late this year.

BUSINESS ACTIVITY - Probably the most significant factors in the manufacturing report for May were significant declines in orders relative to shipments, leading to a negligible further increase in backlog, and a significant increase in inventories for finished goods. The slowing of backlogs suggests that production declines could develop if orders weaken further. The manufacturing figures suggest that an imbalance between anticipated sales and production has developed and almost certainly will lead to further restraints upon production. In other words, several months of weakness in the industrial sector can now be anticipated.

The purchasing managers already indicate that orders probably weakened again in June. Moreover, signs that industrial production and business equipment fell in June suggest that orders for nondefense capital goods may be weakening further. A shrinking backlog is anticipated in that sector before the end of summer.

Industrial production showed weakness in business equipment and consumer goods activity with auto assemblies at only 6.8 million units in June. This should slow the growth of orders. In addition, bottleneck pricing is rapidly dissipating.

PRICES - Construction costs have been revised upward and their rate of increase has also been revised in recent months. This necessitates a more rapid rate of change in the implicit construction deflator than originally generated. Also, these upward revisions suggest that the GNP deflator will be revised upward. No adjustments have been made to reflect that at this time, except to the extent that the construction deflator is now growing at a faster rate.

On the other hand, inflationary forces are rapidly diminishing. The reduction in bottlenecks is clearly reflected in prices of industrial materials. In addition, oil prices appear to be stalled at slightly more than $20 per barrel. In addition, grocery store prices currently are projected to show little change in the second half of this year. Thus, a 48% increase in prices of vegetables from a year ago should actually be reversed slightly. With less pressure for price increases of oil and food products and reduced industrial material pricing pressures, moderation is expected in prices of goods and services. Although prices of consumer nondurables have been growing faster than anticipated early this year, they are now flattening out. Prices of consumer durables also are expected to grow slowly. As a result, the consumption deflator should grow about a half percent more slowly in the next twelve months than originally projected. This moderation of inflation also is anticipated in the CPI and PPI indices.

MISCELLANEOUS - The strong dollar has aided the merchandise trade balance by restraining import prices. However, the flows of imports should gradually intensify later this year. This will be offset to some extent by domestic weakness. The net effect of these crosscurrents is a trade balance that appears stalled between $8 and $9 billion per month. Such a stalled trade balance along with reduced short-term interest rates and weakening profitability in the United States should put downward pressures upon the dollar. The dollar alreay appears to have peaked and should be falling significantly over the next twelve months.

The leading indicators should fall further in June, as sensitive prices and the workweek already have declined. In addition, initial claims have risen significantly and delivery delays have shrunk. The only offsetting force at this time is a further increase in stock market values. The money stock may have ceased declining.

Actual profits probably will be falling significantly as inventory profits are squeezed out of the system. However, this should improve the quality of profits, which had deteriorated significantly during the first half of this year. The stock market's reaction to this improved quality is difficult to gauge, as the market refused to sell off during a period of significant quality erosion. At any rate, as the IVA declines, adjusted profits should remain near current levels despite weakness in industrial activity. On the other hand, after tax profits probably will be down 4% from previous year levels by the end of this year.

FINANCIAL MARKETS

Strong tax collections have led to a reduction in government borrowing requirements. Further moderation in government borrowings is not anticipated through the remainder of this year. However, reductions in defense requirements probably will lead to modestly further declines in borrowings during 1990. On balance, however, the government sector probably will be neutral in influencing interest rate movements over the next year.

The household sector did not increase savings as much as originally anticipated as a result of heavy tax payments, but some improvement did develop. Savings rates may rise slightly later this year, but the household sector on balance probably will preserve current contributions to credit markets. As housing activity will gradually improve, the household sector may be slightly reducing net savings late this year.

The corporate sector already is significantly increasing borrowings in order to finance undesired inventories. In addition, corporate cash flows appear to be under some downward pressures. As the IVA declines, however, corporate borrowing requirements may diminish. Therefore, reductions in corporate borrowing needs could lead to significant declines in interest rate pressures during the second half of this year. Further moderate declines next year also could be anticipated as capital spending programs are contained.

The combined influences of the domestic sector suggest that interest rates could be falling slightly later this year and fall again early next year. Foreign investors may work against such a trend. As the dollar begins losing value, they may desire a withdrawal of funds from the United States. This could put upward pressures upon interest rates. However, they are not expected to dramatically shift portfolios, as alternatives to U.S. capital are not easy to find.

On balance, interest rates should be moving downward this year and next year. However, most of the downward movement probably will be in short-term interest rates, especially as the Federal Reserve finally decides that economic slowing may be greater than they had desired. Such a realization should surface after consumer prices slow to the 4% zone. Thus, by the end of summer, the Federal Reserve should be aggressively pushing short-term interest rates down. There will be little opportunity for further declines in long-term interest rates, as long term investors already are anticipating such a Federal Reserve policy. Nevertheless, long-term government bond yields could fall a half a percentage point over the next twelve months.

The federal funds rate remains well above commercial paper rates. This indicates that the Federal Reserve is not leading the easing movement but is actually lagging behind. Thus, the yield curve remains nearly inverted despite downward movements in interest rates. The Federal Reserve is expected to grudgingly move target rates downward, as the economy continues to perform weakly. The result should be a significant drop in the prime rate before the end of this year.

EQUITY MARKETS - Areas of weakness should include some of the cyclical issues that "soft landing" advocates had been endorsing. For example, profits should be taken in the automotive and metals industries. Buildup of inventories should create some concern about holdings in textiles and furniture. Retail issues should be looked at with care. Until the dollar weakens significantly, multinational issues should remain suspect.

However, interest-sensitive issues, including some construction-related activity, could perform well. While the technology issues are expected to weather earnings embarrassments for the remainder of this year, they should perform better next year. Some of the secondary issues also appear to have merit.

On balance, the stock market appears to be overvalued. A 10% decline in market values from current levels should be anticipated over the next six months. However, further declines in interest rates should prevent any serious downward movement in equity values.

EMPLOYMENT

	Payroll Employment		Index of Hours Worked		Household Civilian Employment		Civilian Unemployment Rate		Hourly Earnings	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	108065	107442	128.3	127.4	116711	116711	5.4	5.4	9.49	9.49
February	108341	107711	127.8	127.2	116853	116853	5.1	5.1	9.50	9.52
March	108512	107888	128.1	127.0	117136	117136	5.0	5.0	9.52	9.54
April	108695	108101	129.5	128.7	117226	117113	5.2	5.3	9.58	9.61
May	108820	108308	128.0	127.6	117363	117215	5.2	5.2	9.62	9.61
June	108946	108488	128.5	127.8	117502	117541	5.1	5.3	9.66	9.62
July	109167	108653*	128.9	128.0*	117743	117713*	5.1	5.3*	9.70	9.66*
August	109384	108829	129.3	128.2	117979	117905	5.0	5.3	9.74	9.69
September	109602	109083	129.7	128.5	118208	118107	5.0	5.2	9.78	9.72
October	109715	109319	129.5	128.8	118328	118367	5.0	5.2	9.82	9.75
November	109832	109508	129.7	129.0	118497	118582	5.1	5.2	9.86	9.78
December	109950	109705	129.9	129.2	118654	118821	5.0	5.1	9.90	9.81
January 1990	110106	109894	130.0	129.4	118827	119022	5.0	5.1	9.94	9.85
February	110303	110007	130.2	129.5	119012	119160	5.0	5.1	9.98	9.88
March	110501	110110	130.3	129.6	119296	119306	5.1	5.2	10.02	9.91
April	110605	110091	130.4	129.5	119337	119236	5.1	5.4	10.06	9.94
May	110636	110043	130.4	129.3	119305	119256	5.2	5.5	10.10	9.98
June	110640	110051	130.3	129.2	119324	119298	5.3	5.7	10.14	10.02

PERSONAL INCOME

	Personal Income		Wage & Salary		Personal Savings		Disposable Income		Personal Outlays	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	4.272	4.273	2.559	2.559	187.9	169.3	3.659	3.639	3.472	3.470
February	4.316	4.318	2.571	2.571	213.7	204.2	3.701	3.687	3.487	3.483
March	4.350	4.356	2.592	2.594	234.0	220.7	3.729	3.716	3.495	3.496
April	4.378	4.377	2.607	2.611	220.8	158.3	3.750	3.692	3.529	3.533
May	4.398	4.390	2.619	2.616	207.9	199.4	3.765	3.744	3.557	3.544
June	4.420	4.408*	2.631	2.624*	206.2	198.9*	3.781	3.759*	3.575	3.560*
July	4.450	4.426	2.649	2.633	214.2	199.1	3.814	3.773	3.600	3.574
August	4.481	4.448	2.667	2.646	211.5	194.6	3.834	3.792	3.623	3.597
September	4.511	4.473	2.685	2.663	218.0	201.4	3.855	3.813	3.637	3.612
October	4.534	4.497	2.699	2.679	219.3	199.3	3.875	3.833	3.656	3.634
November	4.554	4.520	2.709	2.694	221.5	203.3	3.894	3.853	3.673	3.650
December	4.573	4.542	2.719	2.708	226.3	200.8	3.916	3.872	3.690	3.671
January 1990	4.600	4.566	2.738	2.726	227.4	209.2	3.938	3.895	3.711	3.686
February	4.626	4.588	2.759	2.738	227.4	212.3	3.960	3.920	3.733	3.708
March	4.652	4.610	2.780	2.751	227.0	201.4	3.982	3.935	3.755	3.734
April	4.669	4.628	2.791	2.759	223.4	192.4	3.995	3.939	3.772	3.747
May	4.685	4.649	2.801	2.769	216.0	199.4	4.009	3.964	3.793	3.765
June	4.701	4.669	2.810	2.780	214.0	194.7	4.026	3.979	3.812	3.784

Fore. = May Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

CONSUMPTION

	Personal Consumption		Durables		Nondurables		Services		Consumption Real	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	3367.8	3365.4	469.1	467.7	1088.9	1088.8	1809.8	1808.9	2634.1	2632.8
February	3383.2	3378.3	461.0	459.1	1093.9	1091.8	1828.4	1827.4	2641.0	2639.2
March	3390.3	3390.6	454.3	452.8	1098.4	1097.5	1837.6	1840.3	2629.4	2632.8
April	3424.2	3428.0	463.7	472.8	1110.3	1103.3	1850.2	1851.9	2642.1	2643.2
May	3451.8	3438.9	468.5	465.7	1121.2	1104.1	1862.1	1869.1	2651.1	2636.4
June	3469.2	3454.4*	467.6	464.9*	1127.6	1109.1*	1874.0	1880.4*	2652.3	2641.2*
July	3493.8	3468.0	470.3	460.7	1134.3	1114.0	1889.2	1893.3	2660.9	2642.5
August	3516.1	3491.2	473.9	465.5	1138.6	1119.5	1903.6	1906.2	2669.8	2652.7
September	3530.2	3505.1	469.4	461.2	1142.8	1124.3	1918.0	1919.6	2672.4	2653.4
October	3548.4	3526.9	470.6	465.1	1147.3	1129.3	1930.5	1932.5	2674.0	2659.9
November	3564.8	3542.6	469.0	462.0	1152.8	1134.9	1943.0	1945.7	2674.3	2662.1
December	3581.5	3563.7	467.7	465.8	1158.2	1139.5	1955.6	1958.4	2674.8	2669.1
January 1990	3602.4	3578.0	469.9	461.1	1163.6	1145.1	1968.9	1971.8	2680.4	2669.1
February	3624.0	3599.6	472.1	464.5	1169.7	1150.8	1982.2	1984.3	2688.4	2676.0
March	3645.6	3625.2	474.3	470.3	1175.8	1157.5	1995.5	1997.4	2694.5	2684.7
April	3662.2	3637.9	472.7	466.3	1180.2	1161.1	2009.3	2010.5	2694.8	2682.4
May	3683.2	3655.6	475.1	465.3	1183.5	1166.0	2024.6	2024.3	2696.3	2684.9
June	3701.7	3674.9	475.1	467.1	1186.7	1170.2	2039.9	2037.6	2698.0	2690.0

RETAIL SALES

	Retail Sales		Non-Auto Durables		Auto (Million Units)		Nondurable Sales		Auto Sales	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	140.04	140.04	22.62	22.62	9.8	9.8	86.23	86.23	31.19	31.19
February	139.43	139.43	22.43	22.43	9.9	9.9	86.36	86.36	30.64	30.64
March	139.36	139.52	22.13	22.10	9.6	9.6	86.76	86.63	30.48	30.79
April	139.93	140.94	21.83	22.41	10.8	10.8	87.30	87.12	30.81	31.41
May	141.36	140.94	22.34	22.47	10.0	10.2	88.16	87.13	30.86	31.48
June	141.74	141.31*	22.54	22.58*	9.6	9.8	88.66	87.54*	30.54	31.19*
July	142.58	141.21	22.47	22.33	9.8	9.9*	89.19	87.92	30.92	30.96
August	143.33	142.20	21.95	22.17	10.5	10.2	89.53	88.36	31.85	31.67
September	143.15	142.08	21.87	22.11	10.2	10.0	89.86	88.74	31.42	31.23
October	143.63	142.92	22.17	22.20	9.8	9.8	90.21	89.13	31.25	31.59
November	143.88	143.00	22.02	22.06	9.7	9.7	90.64	89.57	31.22	31.37
December	144.16	143.82	21.46	22.13	9.9	9.8	91.07	89.94	31.63	31.75
January 1990	144.83	143.71	21.60	21.87	9.9	9.7	91.49	90.38	31.74	31.46
February	145.56	144.64	21.64	21.98	10.0	9.9	91.97	90.83	31.95	31.83
March	146.29	145.76	21.96	22.14	9.9	10.2	92.45	91.36	31.88	32.26
April	146.46	145.57	21.90	22.05	9.8	10.0	92.80	91.64	31.76	31.88
May	146.99	145.85	21.88	22.18	10.0	9.8	93.06	92.03	32.05	31.64
June	147.24	146.39	21.70	22.21	10.1	9.9	93.31	92.36	32.23	31.82

Fore. = May Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

CONSTRUCTION

	Housing Starts		Single Family Starts		Housing Permits		Construction Expenditures (Current)		Construction Expenditures (Real)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	1.678	1.678	1.199	1.199	1.486	1.486	418.0	424.8	358.9	358.3
February	1.465	1.465	1.029	1.029	1.403	1.403	414.8	418.5	355.7	349.4
March	1.399	1.409	0.986	0.981	1.230	1.230	413.5	419.2	354.2	348.0
April	1.361	1.339	1.015	1.027	1.318	1.334	409.3	415.9	350.1	345.1
May	1.406	1.311	1.021	0.980	1.305	1.336	409.0	421.3	349.6	348.8
June	1.412	1.340*	0.970	0.975*	1.317	1.307*	409.2	415.8*	349.1	343.6*
July	1.354	1.371	0.968	0.993	1.267	1.312	408.3	419.4	347.2	345.5
August	1.342	1.368	0.963	0.996	1.246	1.304	407.2	423.2	345.7	347.7
September	1.327	1.388	0.958	1.011	1.229	1.320	406.0	424.4	344.1	347.6
October	1.335	1.390	0.952	1.015	1.238	1.326	408.6	424.3	345.7	346.7
November	1.340	1.380	0.947	1.006	1.245	1.316	410.8	425.8	347.0	346.7
December	1.343	1.404	0.943	1.012	1.249	1.322	412.9	426.9	348.1	346.2
January 1990	1.296	1.410	0.935	1.023	1.217	1.313	413.0	427.8	347.6	345.8
February	1.304	1.402	0.928	1.005	1.223	1.324	414.1	426.3	348.0	343.5
March	1.321	1.405	0.921	1.022	1.229	1.328	414.1	428.1	347.1	343.9
April	1.327	1.407	0.935	1.023	1.234	1.319	416.0	429.7	348.1	344.0
May	1.335	1.430	0.942	1.036	1.236	1.362	417.7	432.0	348.7	344.5
June	1.343	1.433	0.949	1.038	1.245	1.341	419.5	433.0	349.6	343.9

	Non-Residential		Public Construction		Residential Construction	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	135.1	134.8	81.4	85.3	201.4	204.7
February	133.7	132.7	81.5	83.4	199.6	202.3
March	138.7	135.9	74.1	78.7	200.7	204.5
April	136.6	131.2	76.5	80.8	196.2	203.9
May	136.4	134.4	76.9	86.2	195.7	200.7
June	136.6	132.7*	77.3	83.7*	195.3	199.4*
July	137.0	133.6	77.9	84.6	193.4	201.2
August	137.4	134.6	78.4	85.1	191.4	203.5
September	137.7	135.0	78.8	85.3	189.5	204.1
October	138.5	134.6	79.5	85.2	190.6	204.5
November	139.3	135.3	80.0	86.3	191.5	204.2
December	140.0	136.0	80.5	86.6	192.4	204.3
January 1990	140.3	136.5	80.9	86.9	191.8	204.4
February	140.7	136.1	81.4	85.6	192.0	204.6
March	141.1	136.5	80.8	86.8	192.2	204.8
April	141.5	137.2	81.2	87.2	193.3	205.3
May	141.3	138.0	81.8	87.5	194.6	206.5
June	141.3	138.4	82.3	87.9	195.9	206.7

Fore. = May Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

BUSINESS ACTIVITY

	Manufacturers' Inventories		Durable Goods Orders		Non-Defense Capital Goods Orders		Non-Defense Capital Shipments	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	357.5	357.5	128.48	128.48	40.35	40.35	33.33	33.33
February	359.1	359.1	124.11	124.11	37.19	37.19	33.46	33.46
March	360.4	361.1	125.21	125.38	38.09	38.14	34.03	34.08
April	363.4	363.5	126.63	129.37	37.76	40.39	34.26	34.60
May	365.3	365.5	129.94	123.57	37.85	36.93	34.39	34.47
June	367.2	367.4*	126.27	122.63*	37.12	36.75*	34.52	34.53*
July	370.5	369.5	126.43	124.32	36.69	37.21	34.82	34.76
August	373.4	371.8	126.68	122.76	36.63	35.94	35.03	34.91
September	376.2	374.1	126.29	122.51	36.17	35.56	35.24	35.13
October	378.9	376.5	125.76	123.12	35.84	35.82	35.36	35.29
November	381.1	378.9	125.43	122.65	35.53	35.59	35.45	35.46
December	383.3	381.2	125.89	122.74	35.72	35.62	35.75	35.81
January 1990	385.2	383.7	126.14	121.96	35.88	35.43	35.66	35.56
February	387.4	386.2	126.35	122.15	36.17	35.27	35.87	35.62
March	389.6	388.1	126.12	121.36	35.93	34.65	36.02	34.93
April	390.9	390.4	125.56	121.95	35.76	34.85	36.05	35.13
May	391.3	391.8	124.85	120.98	35.49	34.37	36.01	34.81
June	391.7	393.0	125.18	121.15	34.64	34.12	35.99	34.73

	Business Inventories		Defense Shipments		Industrial Production		Capacity Utilization	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	759.8	759.8	8.73	8.73	140.8	140.8	84.3	84.3
February	763.6	763.1	8.40	8.40	140.4	140.5	83.9	83.9
March	765.6	765.5	8.50	8.45	140.5	140.7	83.7	83.8
April	772.3	769.8	8.58	8.63	140.9	141.6	83.8	84.1
May	779.6	773.5*	8.62	8.69	141.2	141.4	83.9	83.8
June	786.8	778.4	8.62	8.73*	141.5	141.1	84.0	83.5
July	789.9	783.1	8.55	8.70	142.7	141.1	84.4	83.4*
August	793.0	787.5	8.61	8.74	143.9	141.1	84.8	83.3
September	795.9	793.2	8.67	8.81	145.1	141.5	85.2	83.4
October	801.4	798.4	8.62	8.75	144.7	141.9	84.7	83.6
November	808.9	803.1	8.70	8.73	144.3	142.2	84.3	83.7
December	816.3	808.6	8.78	8.84	144.6	142.3	84.4	83.6
January 1990	819.4	814.3	8.68	8.81	144.5	142.4	84.1	83.5
February	822.0	819.2	8.76	8.85	144.2	142.2	83.8	83.1
March	824.6	823.5	8.90	8.90	143.9	142.1	83.5	82.8
April	828.5	827.1	8.74	8.93	143.4	141.8	83.1	82.4
May	832.4	830.6	8.67	8.90	142.9	141.4	82.7	82.0
June	833.2	833.2	8.60	8.86	142.5	141.2	82.4	81.7

Fore. = May Forecast
C.E. = Current Expectations
* = This item and those beyond it are expectations.

PRICES

	CPI-U (seasonally adjusted)		PPI Finished Goods (seasonally adjusted)		PPI-Industrial Commodities (unadjusted)		Estimated GNP Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	121.4	121.4	111.0	111.0	109.1	109.1	125.0	125.0
February	121.9	121.9	112.1	112.1	110.0	110.0	125.2	125.1
March	122.5	122.5	112.6	112.6	110.6	110.6	125.5	125.3
April	123.4	123.3	113.1	113.1	111.3	111.3	126.1	126.1
May	124.1	124.0	113.8	114.1	112.0	111.7	126.8	126.8
June	124.5	124.4*	114.2	114.4*	112.7	111.6*	127.2	127.1
July	125.1	124.8	114.4	114.5	113.0	112.0	127.5	127.5
August	125.6	125.2	114.7	114.7	113.5	112.4	127.9	127.9
September	126.2	125.6	114.7	114.9	112.5	111.6	128.3	128.4
October	126.7	126.1	115.0	115.0	113.9	113.1	128.8	128.8
November	127.2	126.6	115.3	115.4	114.0	113.5	129.3	129.3
December	127.8	127.0	115.6	115.5	114.2	113.9	129.8	129.7
January 1990	128.2	127.5	116.0	115.8	114.8	114.3	130.4	130.3
February	128.5	127.9	116.5	116.1	115.6	114.6	131.0	130.7
March	128.9	128.4	116.8	116.3	116.4	115.0	131.6	131.2
April	129.5	129.0	117.2	116.6	116.8	115.5	132.1	131.8
May	130.2	129.5	117.6	117.0	117.1	115.9	132.7	132.3
June	130.9	129.9	118.1	117.2	117.4	116.3	133.3	132.7

	Consumption Deflator		Consumer Durables		Consumer Nondurables		Consumer Services		Implicit Construction Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	127.9	127.8	112.0	112.0	119.4	119.3	138.9	138 8	116.4	118.6
February	128.1	128.0	111.7	111.5	119.5	119.5	139.2	139.1	116.6	119.8
March	128.9	128.8	111.3	111.1	121.0	120.8	139.9	139.8	116.7	120.4
April	129.6	129.7	111.6	111.4	122.2	122.8	140.5	140.3	116.9	120.5
May	130.2	130.4	111.8	111.6	123.2	123.9	141.1	140.7	117.1	120.8
June	130.8	130.8*	112.0	111.7*	123.6	124.3*	141.7	141.1*	117.3	121.0*
July	131.3	131.2	112.4	112.0	123.8	124.6	142.3	141.6	117.6	121.4
August	131.7	131.6	112.7	112.2	124.0	124.9	142.9	142.1	117.8	121.7
September	132.1	132.1	113.0	112.5	124.2	125.3	143.5	142.6	118.0	122.1
October	132.7	132.6	113.2	112.7	124.8	125.8	144.2	143.2	118.2	122.4
November	133.3	133.1	113.4	113.0	125.3	126.2	144.9	143.7	118.4	122.8
December	133.9	133.5	113.4	113.1	125.9	126.6	145.6	144.3	118.6	123.3
January 1990	134.4	134.1	113.7	113.4	126.3	127.0	146.2	144.9	118.8	123.7
February	134.8	134.5	114.0	113.6	126.6	127.4	146.9	145.5	119.0	124.1
March	135.3	135.0	114.3	114.0	127.0	127.9	147.5	146.1	119.3	124.5
April	135.9	135.6	114.4	114.2	127.7	128.5	148.3	146.7	119.5	124.9
May	136.6	136.2	114.5	114.4	128.4	129.0	149.0	147.3	119.8	125.4
June	137.2	136.6	114.4	114.5	129.0	129.4	149.7	147.9	120.0	125.9

Fore. = May Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

MISCELLANEOUS

	Merchandise Trade Balance		Leading Indicators	Estimated GNP		Estimated GNP (1982 $)		IVA (annual rate)	
	Fore.	C.E.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	-8.68	-8.68	146.1	5109	5090	4087	4072	-26.7	-26.7
February	-9.82	-9.82	145.5	5114	5099	4085	4076	-39.6	-39.6
March	-8.86	-8.86	144.6	5127	5108	4085	4077	-41.7	-42.2
April	-9.73	-8.26	145.5	5163	5146	4094	4081	-40.2	-45.3
May	-9.92	-8.64*	143.8	5197	5173	4099	4080	-28.6	-38.4
June	-9.42	-9.13	143.5*	5231	5195	4112	4087	-23.5	-34.6
July	-10.21	-9.53	144.1	5256	5216	4122	4091	-25.5	-27.9
August	-10.88	-8.87	143.8	5288	5251	4134	4106	-28.0	-23.4
September	-10.83	-9.22	143.9	5320	5280	4147	4112	-29.9	-16.8
October	-10.62	-9.17	144.3	5341	5306	4147	4120	-28.6	-14.3
November	-10.25	-8.55	143.7	5359	5331	4145	4123	-27.4	-11.5
December	-9.56	-8.46	143.3	5379	5355	4147	4129	-26.3	-13.4
January 1990	-9.93	-8.92	142.9	5405	5380	4145	4129	-30.2	-18.1
February	-10.58	-9.43	143.2	5442	5411	4154	4140	-32.4	-18.3
March	-10.86	-9.26	142.7	5480	5439	4164	4146	-34.6	-15.7
April	-9.85	-9.25	143.0	5493	5458	4158	4141	-31.1	-16.5
May	-9.52	-9.45	142.8	5502	5473	4146	4137	-29.9	-18.8
June	-9.37	-9.16	143.0	5508	5496	4132	4142	-28.7	-21.4

	Currency Index		Adjusted Profits		30-Year Government Bonds		New York Composite	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	95.12	95.12	210.5	193.6	8.93	8.93	160.40	160.40
February	95.77	95.77	163.4	163.9	9.01	9.01	165.08	165.08
March	96.99	96.99	156.5	156.4	9.17	9.17	164.60	164.60
April	97.23	97.24	165.9	159.8	9.32	9.03	165.13	170.34
May	97.95	100.81	178.2	154.7	9.40	8.83	166.29	175.56
June	98.56	103.09	180.3	165.2	9.36	8.28*	164.21	180.90
July	97.43	99.76*	177.4	165.8	9.30	8.03	156.82	188.62*
August	95.82	97.24	175.7	169.6	9.25	7.86	153.54	191.11
September	94.16	96.62	174.0	172.2	9.21	7.93	150.26	188.37
October	93.09	95.43	173.1	168.3	9.18	8.11	148.29	189.57
November	91.70	93.48	172.4	166.5	9.12	7.89	148.86	182.77
December	90.36	94.12	171.9	163.3	9.15	7.75	149.30	182.49
January 1990	91.25	94.55	169.8	165.1	9.06	7.82	145.14	172.83
February	94.46	94.83	169.1	164.6	9.01	7.84	140.53	171.87
March	94.05	93.64	168.2	170.3	8.92	7.65	138.27	182.24
April	91.02	92.26	168.5	167.2	8.78	7.63	139.45	179.39
May	89.63	92.85	166.1	165.3	8.73	7.55	140.25	179.23
June	88.26	91.16	163.7	167.8	8.70	7.53	141.06	182.10

Fore. = May Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

FINANCIAL MARKETS

	Monetary Base		M1		M2		Federal Funds		T-Bills (6 Mos.)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	287.9	287.9	786.3	786.3	3065.9	3065.7	9.12	9.12	8.36	8.36
February	287.5	287.5	787.4	787.4	3069.7	3069.2	9.36	9.36	8.55	8.55
March	289.4	289.3	786.3	786.3	3079.5	3078.7	9.85	9.85	8.85	8.85
April	290.3	289.1	782.9	783.2	3090.4	3081.3	9.84	9.84	8.65	8.65
May	292.9	289.0	785.3	773.4	3101.3	3072.8	9.83	9.81	8.74	8.39
June	295.5	289.6*	787.2	770.8	3112.2	3090.0	9.83	9.47*	8.83	8.04*
July	297.3	289.9	792.5	775.5*	3134.6	3107.4*	10.20	9.11	8.89	7.88
August	298.1	292.4	798.9	780.9	3158.6	3129.0	10.23	8.86	8.86	7.76
September	298.9	293.6	804.9	784.0	3182.5	3141.4	10.26	8.78	8.83	7.71
October	300.4	295.5	808.6	788.3	3195.6	3158.6	10.32	8.73	8.81	7.65
November	302.8	297.2	812.4	793.5	3213.2	3179.4	10.29	8.52	8.82	7.43
December	305.2	298.3	816.2	798.7	3231.0	3200.2	10.26	8.29	8.80	7.29
January 1990	306.9	299.9	821.7	803.3	3250.4	3218.6	10.01	8.27	8.73	7.23
February	307.8	300.8	828.6	806.1	3270.3	3235.8	9.96	8.20	8.62	7.15
March	308.7	302.1	835.4	810.9	3290.1	3255.1	9.84	8.11	8.51	7.06
April	310.5	304.0	840.3	814.9	3314.3	3271.2	9.56	7.96	8.47	6.89
May	312.5	305.7	845.0	818.8	3326.1	3286.9	9.55	7.93	8.41	6.87
June	314.4	307.5	849.8	822.7	3338.0	3302.6	9.56	7.85	8.36	6.84

	Aaa (Seasoned)		Municipals (Bond Buyer)		(3 Month) Commercial Paper		90 Day CD's		Prime Rate	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	9.62	9.62	7.35	7.35	9.04	9.04	9.20	9.20	10.50	10.50
February	9.64	9.64	7.44	7.44	9.37	9.37	9.51	9.51	10.93	10.93
March	9.80	9.80	7.59	7.59	9.95	9.95	10.09	10.09	11.50	11.50
April	9.79	9.79	7.49	7.49	9.81	9.81	9.94	9.94	11.50	11.50*
May	9.75	9.57	7.45	7.25	9.80	9.47	9.93	9.59	11.50	11.50
June	9.83	9.20*	7.51	7.03*	9.86	9.12*	9.97	9.32*	11.50	11.07
July	9.89	8.96	7.58	6.87	10.17	8.96	10.26	9.16	11.68	10.68
August	9.95	8.89	7.64	6.75	10.26	8.76	10.35	8.98	12.00	10.50
September	9.99	9.02	7.68	6.86	10.23	8.75	10.30	8.95	12.00	10.50
October	9.90	9.15	7.62	7.01	10.30	8.79	10.41	8.96	12.00	10.50
November	9.83	9.14	7.53	6.97	10.25	8.53	10.37	8.77	12.00	10.50
December	9.76	8.96	7.47	6.91	10.22	8.28	10.33	8.53	12.00	10.41
January 1990	9.70	8.84	7.40	6.77	10.07	8.23	10.22	8.46	12.00	10.00
February	9.67	8.79	7.38	6.68	9.98	8.18	10.09	8.37	11.96	10.00
March	9.64	8.62	7.35	6.65	9.88	8.04	10.05	8.29	11.50	10.00
April	9.56	8.53	7.26	6.59	9.59	7.99	9.76	8.21	11.50	10.00
May	9.53	8.49	7.20	6.50	9.53	7.95	9.71	8.16	11.28	10.00
June	9.50	8.43	7.18	6.46	9.50	7.89	9.65	8.09	11.00	10.00

Fore. = May Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

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ECONOMIC FORECASTING CENTER

MONTHLY PROJECTIONS
July 1989

Dr. Donald Ratajczak, Director
For Release: Thursday, August 17, 1989

WHERE ARE THE ECONOMIC IMBALANCES?

Early this year, all the early signals of an impending recession appeared to be in place. Commodity prices were rising rapidly. Inventory profits were growing sharply. Short-term interest rates were surging and had outpaced long-term interest rates. Although the surge in inventory profits masked a deterioration in corporate profitability, cost-cutting soon would develop when commodity inflation slowed and revealed the crunch in operating profits that occurred during the first quarter. Even the dollar's rally, which significantly reduced potential for export growth, indicated that industrial problems were ahead. Despite strong growth in stock prices, the leading indicators confirmed that these signals revealed stormy economic clouds ahead.

Initially, some signs of economic imbalance also appeared to be developing. Inflation-adjusted nonfarm inventories appeared to have grown by $41 billion during the first quarter. This was following a slightly excessive rate of inventory accumulation last year. With consumer purchases sagging under the onslaught of rising commodity prices, weakening in final sales soon could lead to excessive inventory holdings that almost always precedes a recession.

However, data revisions show that those inventory accumulations were overstated. Inventories grew $15 billion less in 1988 than originally reported. More significantly, the $41 billion surge in inventories during the first quarter was scaled back to a modest gain of only $17 billion. While inventories spurted in the middle of the second quarter, especially as consumers shunned automobiles, manufacturers were quick to adjust to reduced order flows. By the end of the quarter, inventories once again were being accumulated at a rate consistent with recently anticipated sales growth.

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Even trade imbalances improved as a result of a $35 billion upward adjustment in inflation-adjusted exports. Although the current account deficit remains in the $100 billion range, this is down considerably from the more than $130 billion previously estimated. Much of the improvement was in exported services, leading to better productivity gains in the service sector than originally anticipated. Indeed, as a result of this upward revision in service exports, overall productivity during the past three years has averaged a satisfactory 1.8%. In 1988, productivity in the private economy grew 1.2% despite serious drought-related productivity problems in the farm economy. Such productivity improvement indicates that an upward drift in wage costs has been met by an upward drift in productivity.

In short, if current economic data is more accurate than the data previously reported, there are no serious economic imbalances that normally develop prior to a recession.

This year's price fluctuations provide clues as to how supply shocks change inflation. No one would deny that petroleum oil restraints or droughts would have an impact upon petroleum prices and food prices. These "supply shocks" occurred last year and generated their appropriate surges in prices in the relevant sectors. However, Dr. Milton Friedman has argued on several occasions that such supply conditions only change relative prices. As he is fond of quoting, "inflation is everywhere and always a monetary phenomenon". From the pricing behavior observed this year, that statement must be amended to end with the phrase "in the long run." In the relevant short-run, increasing price pressures for oil and food products do not cause other producers to run out and slash their prices. Instead, those price increases must crowd out purchasing power. A reduction in sales of other goods then must lead to the price concessions that ultimately lead to only a relative price movement in the absence of monetary ratification of the supply shocks.

Of course, what normally occurs is monetary ratification. Federal Reserves in the past have used interest rate targets to dictate their monetary policy. When a supply shock occurred, the resulting increases in prices led to tightening credit market pressures. The surge in inventory profits generated early this year was largely the result of last year's supply shock. The borrowings necessary to support those inventories led to rising short-term interest rates. Federal Reserves with interest rate targets will inappropriately read rising interest rates as a tightening of monetary policy. They, then, would increase growth in the monetary aggregates, leading to monetary support for the supply shocks. As a result, inflation increases.

This Federal Reserve decided not to monetize the drought and oil shocks. As a result, rising commodity prices reduced consumer purchasing power while rising short-term interest rates slowed the interest-sensitive parts of the economy. Production weakness then caused prices to grow by less than otherwise would have occurred. Indeed, inflation probably will now run below trend rates for much of the second half of this year, following above trend rates of inflation in the first six months. By year's end, the supply shocks will have only changed relative prices, as Dr. Friedman asserts.

Now that the surging portion of commodity prices has ended, the dip in commodity prices that should be observed will stimulate consumer spending. (A one-time surge in tax collections also restrained consumer spending during the second quarter, which now should be reversed in the second half of the year.) In short, the decline in commodity prices suggests that enough production slowing already has occurred to continue the adjustment process associated with the price run-up from the drought and oil production restraints. Thus, no further serious production reductions appear in store.

None of this suggests that the economy is no longer prone to recessions. Indeed, tight labor markets still could create wage pressures leading to profits imbalances and subsequent cost-cutting. However, such labor imbalances have not yet developed.

Quarterly Profile of GNP

	1989-1	1989-2	1989-3	1989-4	1990-1	1990-2	1989 Annual	1990 Annual
Real:	3.7	1.7	2.3	2.0	1.2	1.1	2.8	1.5
Price:	4.0	4.9	2.9	4.5	4.8	3.8	4.2	4.4
Nominal:	7.9	6.6	5.3	6.7	6.1	5.0	7.1	6.0

Monthly Statistical Highlights

	July 1989	Aug 1989	Sept 1989
Payroll Employment		+186,000	+211,000
Index of Hours Worked		-0.2%	+0.2%
Household Employment		+357,000	+216,000
Civilian Unemployment Rate		5.3%	5.2%
Personal Income	+0.8%	+0.4%	+0.5%
Savings Rate	5.8%	5.7%	5.7%
Personal Consumption	+1.0%	+0.6%	+0.5%
Retail Sales		+0.5%	+0.3%
Auto Sales		10.7*	10.5*
Housing Starts		+0.1%	-1.3%
Housing Permits		-0.6%	+1.2%
Construction Expenditures	+0.9%	+1.2%	-0.5%
Business Inventories	+0.4%	+0.5%	+0.4%
Orders for Durable Goods	+0.6%	-0.9%	-1.1%
Orders - Nondefense Capital Goods	+0.2%	-0.8%	-1.6%
Industrial Production	+0.3%	+0.2%	+0.2%
CPI	+0.1%	+0.2%	+0.4%
PPI		UNC	+0.9%
Consumption Deflator	+0.1%	+0.3%	+0.3%
Leading Indicators	+0.4%	+0.2%	-0.3%
Currency Index		-2.6%	+1.4%
Equity Index		+1.3%	+1.7%
Real GNP (annual rate)	+5.1%	+2.3%	+2.6%
M1 (annual rate)		-0.6%	+4.7%
M2 (annual rate)		+6.4%	+6.3%

* auto sales in millions

COMMENTARY

EMPLOYMENT - The employment report was strong in July. Although the 169,000 increase was far below the 250,000 in the previous month, the composition of that increase was far better. First, the private economy expanded 194,000 jobs. Second, jobs for production workers in manufacturing increased 20,000. Especially impressive was a sharp increase in the private workweek that led to a surge in the index of hours worked. The only part of the report that was weak was in civilian employment, which declined. A spurt in employment probably will occur next month. Hourly earnings spurted, but this index is not adjusted for composition shifts. Thus, an improvement in production workers automatically would have increased the index. Although some wage pressures undoubtedly are being generated, too much has been made of the 0.7% increase in the index for July. Smaller increases should be expected in the summer months. The reduction in unemployment came in the teenage group, as the summer labor force did not swell as much as normally occurs. Longer workweeks suggest stronger payroll employment next month. In addition, the rise in hourly earnings and a sharp increase in the index of hours worked suggest that a very strong gain will be generated for wages and salaries in July.

PERSONAL INCOME AND OUTLAYS - Auto sales rebounded as a result of incentives and a growing attempt to avoid large price increases in the new model year. Almost certainly, there will be a shift in auto sales to the summer months at the expense of the fall. This will have some adverse effects upon consumer spending in the fall and will bolster consumer spending during the summer. Presumably, the automobile industry is aware of these shifts and will not alter production to meet near-term spurts in sales. As a result, only inventory levels will be adjusted by this activity.

However, some analysts were incorrect in assessing that the 0.4% gain in retail sales excluding automobiles in July merely reflected inflation. Indeed, there is no commodity inflation in July. Thus, real consumer sales are surging both in the nondurable and service sectors. The service sector was especially restrained in June as a result of mild and wet weather that sharply reduced normal utility consumption. More normal utility activity in July should lead to a surge there. Thus, consumer activity will spurt in July in addition to the automobile components. The rebound in housing activity probably assures some growth in sales of non-auto durables. Activity improved modestly in July after a sharp upward revision in the May levels. Sharp upward revisions also occurred in the May estimates of nondurable sales to more appropriately reflect sharp petroleum price increases that developed at that time. Now that inflationary pressures are easing and the spring surge in tax payments has moderated, stronger consumer spending is anticipated. Even so, the rebound in wage and salary earnings in July suggests that savings rates will remain relatively high, at 5.8%.

Farm income continued to fall in July but should begin rebounding as the new harvest arrives in September. This will add to further personal income growth and generate some improved savings at that time.

CONSTRUCTION - Declining mortgage rates are beginning to encourage some improvement in housing activity. However, housing permits remain weak, suggesting no dramatic surge in the housing market. Also, single-family starts are only grudgingly increasing. The July figures show that activity weakened in the West and the South while rebounding in the Northeast and Midwest. In the previous month, strength was in exactly the opposite geographic areas. This suggests that sampling problems rather than any substantial shift in momentum currently is developing, although the housing boom in the West may be grinding to a halt.

Some improvement in housing activity should be reflected in improving residential construction activity. The weather also has become more favorable for construction. On the other hand, the June increase in nonresidential construction was broad-based and a surprise. Perhaps, construction teams were more able to do internal work on large projects while weather was denying access to housing production. This normally is not observed, but could suggest that nonresidential construction took a temporary blip and will settle back in the summer months.

Construction costs slowed their rate of ascent in June and probably will grow at a relatively modest rate for the remainder of this year. However, the construction deflator probably will increase in the range of 4%.

BUSINESS ACTIVITY - Manufacturers' inventories grew slowly. As a result, business inventories are now growing significantly slower than had been projected despite continuing accumulations of auto inventories. Thus, most of the production weakness during the spring appears to be the result of managing inventories and therefore is positive for the trend of future economic activity.

Defense activity was stronger than anticipated, but this is probably a temporary spurt. Shipments of nondefense capital goods slowed in June but should grow strongly into next year. Although orders excluding aircraft are only $400 million above shipments, that gap is sufficient for backlogs other than aircraft to grow. No significant correction in shipments are anticipated until the backlog actually begins declining. Primary metals orders should fall following a surge earlier this year. Fortunately, machinery orders have again strengthened following a spring lull. Concern now is in the information equipment area, where customers apparently are waiting for new technology and are not aggressively making commitments. Relatively flat orders should develop through the remainder of this year.

The dip in industrial production probably ended in June as a result of improvement in production worker activity. Weakness was widespread and included business equipment as well as utilities. However, a dip in materials production suggested an attempt to control inventories. Production now should rebound in the next few months. Capacity utilization should remain near current levels with no significant generation of bottlenecks over the next 12 months.

PRICES - As mentioned above, above-trend increases in prices as a result of supply shocks should be followed by below-trend activity if the Federal Reserve does not ratify the supply shocks. This Federal Reserve clearly has not supported the price increases generated by drought and oil production restraints. As a result, commodity prices now are falling significantly. Some declines are in the same areas that showed significant increases, but other declines also are occurring. If the Federal Reserve does not significantly increase money growth, several months of below-trend inflation should be anticipated. Indeed, the CPI for July could remain unchanged. Because of earlier rebates than seasonally anticipated, the auto price indices for July were especially restrained. When the September indices arrive, the price decreases that will be anticipated already will be in place. As a result, a spurt in measured inflation could occur at that time.

A second problem that some people are seeing in the auto area will not materialize. Traditionally, if price changes are the result of mandated regulations, they are viewed as improvements and do not add to the price index. They do add to the ticket price of the car, however. Apparently, the large price increases for automobiles this October will almost all be counted as quality adjustments. Thus, those price increases will not have an impact upon the price indices.

MISCELLANEOUS - Rising oil prices have resulted in a spurt in the trade deficit. In addition, the strong dollar has slowed the flow of exports. Imports are expected to remain strong while a strong dollar will continue to have some adverse effects upon export activity into the fall. Nevertheless, merchandise trade balances should again gradually recede.

The leading indicators should rebound in July as a result of stronger money growth, improving stock values, and modest improvement in orders being only partially offset by initial claims and sensitive prices.

The inventory valuation adjustment will come down as rapidly as it increased as a result of the compression in commodity inflation. As a result, the quality of profits should improve significantly. However, the stock market apparently ignored deterioration in profit quality during the spring and therefore should not rally significantly as quality improves.

FINANCIAL MARKETS

Because of unusual tax collections, the government deficit was surprisingly subdued in the first half of the year. Total government deficits, including the state and local pension surpluses, fell below $100 billion. A rebound to the vicinity of $130 billion is anticipated by the fourth quarter. Then, generally flat borrowing needs are anticipated through 1990. Government borrowings will generate higher interest rates during the summer months followed by a neutral impact upon interest pressures for the remainder of the year.

During the spring, the household sector was able to increase savings even as it was paying heavy taxes as a result of reduced spending programs. This was especially remarkable as commodity prices were significantly raising the costs of consumer goods. During the summer, falling commodity prices should allow the household sector to maintain its savings pattern, although shifting auto sales from the fall to the summer could put some modest upward pressures upon credit markets during that time. Then, of course, reduced auto spending should reduce credit market pressures in the fall.

As usual, most of the borrowing pressures are being generated by the corporate sector. Profitability fell sharply in the first quarter after removing inventory profits. Indeed, corporate savings fell while corporate investment rose because of higher inventory prices. As economic activity picks up modestly in the second half of the year, corporate profits may rebound more significantly. Corporate investment is expected to continue rebounding as a result of higher inventory investments and increased capital spending programs. Capital spending may weaken in the fourth quarter, however.

This suggests that credit market pressures should show surprising strength during the summer. That could lead to a slight rebound in interest rates. Of course, the Federal Reserve probably will not allow an interest rate surge because of previous softness in production. Therefore, money growth probably will rebound, causing some uneasiness for long-term investors. However, these borrowing forces are expected to again ease in the fall, leading to further declines in interest rates into the first half of 1990.

Of course, foreign investors will also be significant in these interest rate movements. With the dollar remaining relatively strong in the summer months, foreigners are offsetting domestic pressures for higher interest rates. By the fall, the domestic pressures should be easing while an anticipated decline in the dollar should discourage foreign investors. Therefore, the decline in interest rates in the fall should be modest. But a decline is anticipated.

EQUITY MARKETS - Equities are overvalued, but they are not that much overvalued. A decline in interest rates justifies most of the upward movement that has been experienced in equity values in the first half of this year. However, the stock market appears to have ignored the deteriorating quality in profits. While the quality of profits should improve in the second half as inventory valuation adjustments decline, the stock market probably will continue to look at after-tax profits. They are expected to fall more than 2% this year and also decline modestly next year. For that reason, equity values are expected to fall in the next six months. Nevertheless, the degree of decline should be modest.

The movement toward cyclical stocks because of the absence of a recession appears to be inappropriate. The inventory profits generated by commodity producers are one-time events that will rapidly vanish. Indeed, some of those industries may have cash-flow problems. Certainly, the primary metals and some of the machinery industries could experience some earnings surprises in the next six months. A safer procedure would be to invest in some of the service-related activities, including entertainment and communications services, and the related peripheral equipment. Early next year, technology companies probably will be in a position to rebound as new technology becomes available. In short, the stock market will be much more selective and show little direction from current levels over the next twelve months.

EMPLOYMENT

	Payroll Employment		Index of Hours Worked		Household Civilian Employment		Civilian Unemployment Rate		Hourly Earnings	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	108065	107442	128.3	127.4	116711	116711	5.4	5.4	9.49	9.49
February	108341	107711	127.8	127.2	116853	116853	5.1	5.1	9.50	9.52
March	108512	107888	128.1	127.6	117136	117136	5.0	5.0	9.52	9.54
April	108695	108101	129.5	128.7	117226	117113	5.2	5.3	9.58	9.61
May	108820	108310	128.0	127.6	117363	117215	5.2	5.2	9.62	9.60
June	108946	108560	128.5	128.0	117502	117541	5.1	5.3	9.66	9.62
July	109167	108729	128.9	129.4	117743	117459	5.1	5.2	9.70	9.69
August	109384	108915*	129.3	129.2*	117979	117816*	5.0	5.3*	9.74	9.72*
September	109602	109126	129.7	129.4	118208	118032	5.0	5.2	9.78	9.75
October	109715	109319	129.5	129.5	118328	118382	5.0	5.1	9.82	9.79
November	109832	109528	129.7	129.8	118497	118552	5.1	5.1	9.86	9.82
December	109950	109705	129.9	129.9	118654	118721	5.0	5.1	9.90	9.85
January 1990	110106	109894	130.0	129.9	118827	118922	5.0	5.1	9.94	9.88
February	110303	110007	130.2	130.0	119012	119064	5.0	5.1	9.98	9.92
March	110501	110110	130.3	130.0	119296	119153	5.1	5.3	10.02	9.95
April	110605	110291	130.4	130.3	119337	119357	5.1	5.3	10.06	9.98
May	110636	110443	130.4	130.7	119305	119527	5.2	5.3	10.10	10.01
June	110640	110607	130.3	130.8	119324	119635	5.3	5.4	10.14	10.05

PERSONAL INCOME

	Personal Income		Wage & Salary		Personal Savings		Disposable Income		Personal Outlays	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	4.272	4.273	2.559	2.545	187.9	174.6	3.659	3.642	3.472	3.467
February	4.316	4.320	2.571	2.557	213.7	210.7	3.701	3.698	3.487	3.487
March	4.350	4.361	2.592	2.579	234.0	231.9	3.729	3.729	3.495	3.497
April	4.378	4.387	2.607	2.601	220.8	183.3	3.750	3.718	3.529	3.535
May	4.398	4.395	2.619	2.602	207.9	203.5	3.765	3.747	3.557	3.543
June	4.420	4.407	2.631	2.616	206.2	224.1	3.781	3.769	3.575	3.545
July	4.450	4.443*	2.649	2.644*	214.2	222.1*	3.814	3.801*	3.600	3.579*
August	4.481	4.461	2.667	2.653	211.5	216.4	3.834	3.815	3.623	3.599
September	4.511	4.484	2.685	2.666	218.0	218.2	3.855	3.836	3.637	3.618
October	4.534	4.508	2.699	2.681	219.3	223.2	3.875	3.856	3.656	3.633
November	4.554	4.531	2.709	2.696	221.5	221.6	3.894	3.875	3.673	3.653
December	4.573	4.551	2.719	2.707	226.3	219.9	3.916	3.891	3.690	3.671
January 1990	4.600	4.567	2.738	2.717	227.4	203.8	3.938	3.892	3.711	3.688
February	4.626	4.593	2.759	2.732	227.4	219.0	3.960	3.928	3.733	3.709
March	4.652	4.613	2.780	2.742	227.0	206.1	3.982	3.938	3.755	3.732
April	4.669	4.640	2.791	2.759	223.4	189.0	3.995	3.937	3.772	3.748
May	4.685	4.668	2.801	2.777	216.0	206.9	4.009	3.973	3.793	3.766
June	4.701	4.691	2.810	2.792	214.0	231.8	4.026	4.013	3.812	3.781

Fore. = May Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

CONSUMPTION

	Personal Consumption		Durables		Nondurables		Services		Consumption Real	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	3367.8	3365.6	469.1	473.1	1088.9	1093.8	1809.8	1798.7	2634.1	2636.5
February	3383.2	3384.7	461.0	464.2	1093.9	1098.6	1828.4	1821.9	2641.0	2647.0
March	3390.3	3394.0	454.3	461.8	1098.4	1102.5	1837.6	1829.6	2629.4	2639.6
April	3424.2	3432.2	463.7	477.3	1110.3	1113.2	1850.2	1841.7	2642.1	2652.5
May	3451.8	3440.2	468.5	467.7	1121.2	1118.1	1862.1	1854.4	2651.1	2647.8
June	3469.2	3441.4	467.6	466.0	1127.6	1118.5	1874.0	1856.9	2652.3	2644.3
July	3493.8	3475.1*	470.3	475.2*	1134.3	1126.6*	1889.2	1873.3*	2660.9	2668.1*
August	3516.1	3494.4	473.9	479.9	1138.6	1128.3	1903.6	1886.2	2669.8	2675.9
September	3530.2	3513.2	469.4	479.7	1142.8	1133.9	1918.0	1899.6	2672.4	2682.0
October	3548.4	3527.7	470.6	476.4	1147.3	1138.8	1930.5	1912.5	2674.0	2684.0
November	3564.8	3547.7	469.0	478.4	1152.8	1143.6	1943.0	1925.7	2674.3	2689.1
December	3581.5	3564.9	467.7	480.4	1158.2	1148.1	1955.6	1936.4	2674.8	2692.7
January 1990	3602.4	3581.4	469.9	479.5	1163.6	1152.0	1968.9	1949.9	2680.4	2694.7
February	3624.0	3601.6	472.1	482.8	1169.7	1157.2	1982.2	1961.6	2688.4	2701.5
March	3645.6	3623.9	474.3	487.7	1175.8	1162.0	1995.5	1974.2	2694.5	2709.0
April	3662.2	3639.7	472.7	485.3	1180.2	1167.9	2009.3	1986.5	2694.8	2710.7
May	3683.2	3657.3	475.1	486.2	1183.5	1172.3	2024.6	1998.8	2696.3	2713.8
June	3701.7	3671.8	475.1	484.9	1186.7	1176.1	2039.9	2010.8	2698.0	2712.9

RETAIL SALES

	Retail Sales		Non-Auto Durables		Auto (Million Units)		Nondurable Sales		Auto Sales	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	140.04	140.04	22.62	22.62	9.8	9.8	86.23	86.23	31.19	31.19
February	139.43	139.43	22.43	22.43	9.9	9.9	86.36	86.36	30.64	30.64
March	139.36	139.52	22.13	22.10	9.6	9.6	86.76	86.63	30.48	30.79
April	139.93	140.94	21.83	22.41	10.8	10.8	87.30	87.12	30.81	31.41
May	141.36	142.54	22.34	22.97	10.0	10.1	88.16	88.40	30.86	31.17
June	141.74	142.44	22.54	22.79	9.6	9.9	88.66	88.79	30.54	30.86
July	142.58	143.73	22.47	22.89	9.8	10.2	89.19	89.16	30.92	31.68
August	143.33	144.41*	21.95	22.88*	10.5	10.7*	89.53	89.30*	31.85	32.23*
September	143.15	144.82	21.87	23.03	10.2	10.5	89.86	89.74	31.42	32.05
October	143.63	144.84	22.17	23.12	9.8	9.6	90.21	90.13	31.25	31.59
November	143.88	145.44	22.02	23.16	9.7	9.7	90.64	90.51	31.22	31.77
December	144.16	146.03	21.46	23.22	9.9	9.8	91.07	90.86	31.63	31.95
January 1990	144.83	146.23	21.60	23.20	9.9	9.7	91.49	91.17	31.74	31.86
February	145.56	147.02	21.64	23.31	10.0	9.9	91.97	91.58	31.95	32.13
March	146.29	147.96	21.96	23.34	9.9	10.2	92.45	91.96	31.88	32.66
April	146.46	148.16	21.90	23.45	9.8	10.0	92.80	92.43	31.76	32.28
May	146.99	148.61	21.88	23.48	10.0	10.0	93.06	92.78	32.05	32.35
June	147.24	148.76	21.70	23.53	10.1	9.9	93.31	93.08	32.23	32.15

Fore. = May Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

CONSTRUCTION

	Housing Starts		Single Family Starts		Housing Permits		Construction Expenditures (Current)		Construction Expenditures (Real)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	1.678	1.678	1.199	1.199	1.486	1.486	418.0	424.8	358.9	358.3
February	1.465	1.465	1.029	1.029	1.403	1.403	414.8	418.5	355.7	349.4
March	1.399	1.409	0.986	0.981	1.230	1.230	413.5	419.2	354.2	348.0
April	1.361	1.343	1.015	1.029	1.318	1.334	409.3	415.8	350.1	345.0
May	1.406	1.309	1.021	0.977	1.305	1.347	409.0	418.2	349.6	346.2
June	1.412	1.400	0.970	0.975	1.317	1.300	409.2	414.7	349.1	342.7
July	1.354	1.388*	0.968	0.970*	1.267	1.312*	408.3	418.5*	347.2	345.0*
August	1.342	1.389	0.963	0.986	1.246	1.304	407.2	423.6	345.7	348.4
September	1.327	1.371	0.958	0.993	1.229	1.320	406.0	421.7	344.1	345.7
October	1.335	1.396	0.952	1.005	1.238	1.326	408.6	424.4	345.7	346.7
November	1.340	1.392	0.947	0.996	1.245	1.316	410.8	425.4	347.0	346.4
December	1.343	1.404	0.943	1.002	1.249	1.322	412.9	427.7	348.1	347.4
January 1990	1.296	1.410	0.935	1.013	1.217	1.313	413.0	428.9	347.6	347.3
February	1.304	1.409	0.928	1.005	1.223	1.324	414.1	430.4	348.0	347.4
March	1.321	1.405	0.921	1.002	1.229	1.328	414.1	431.5	347.1	346.9
April	1.327	1.407	0.935	1.013	1.234	1.319	416.0	432.3	348.1	346.1
May	1.335	1.430	0.942	1.026	1.236	1.362	417.7	434.6	348.7	346.8
June	1.343	1.433	0.949	1.028	1.245	1.341	419.5	435.5	349.6	346.2

	Non-Residential		Public Construction		Residential Construction	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	135.1	134.8	81.4	85.3	201.4	204.7
February	133.7	132.7	81.5	83.4	199.6	202.3
March	138.7	135.9	74.1	78.7	200.7	204.5
April	136.6	131.4	76.5	80.4	196.2	204.0
May	136.4	133.3	76.9	84.7	195.7	200.2
June	136.6	136.1	77.3	80.6	195.3	197.9
July	137.0	135.6*	77.9	82.6*	193.4	200.3*
August	137.4	135.8	78.4	83.1	191.4	204.7
September	137.7	136.0	78.8	83.3	189.5	202.4
October	138.5	136.6	79.5	83.8	190.6	204.0
November	139.3	136.8	80.0	84.3	191.5	204.3
December	140.0	137.1	80.5	84.6	192.4	206.0
January 1990	140.3	137.5	80.9	85.1	191.8	206.3
February	140.7	138.1	81.4	85.0	192.0	207.3
March	141.1	138.5	80.8	85.8	192.2	207.2
April	141.5	138.2	81.2	86.2	193.3	207.9
May	141.3	139.0	81.8	86.5	194.6	209.1
June	141.3	139.4	82.3	86.9	195.9	209.2

Fore. = May Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

BUSINESS ACTIVITY

	Manufacturers' Inventories		Durable Goods Orders		Non-Defense Capital Goods Orders		Non-Defense Capital Shipments	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	357.5	357.5	128.48	128.48	40.35	40.35	33.33	33.33
February	359.1	359.1	124.11	124.11	37.19	37.19	33.46	33.46
March	360.4	361.1	125.21	125.38	38.09	38.14	34.03	34.08
April	363.4	363.5	126.63	129.37	37.76	40.39	34.26	34.60
May	365.3	365.1	129.94	123.68	37.85	37.29	34.39	34.53
June	367.2	366.2	126.27	124.19	37.12	37.39	34.52	34.59
July	370.5	368.1*	126.43	124.94*	36.69	37.47*	34.82	34.76*
August	373.4	370.2	126.68	123.82	36.63	37.17	35.03	34.91
September	376.2	372.1	126.29	122.51	36.17	36.56	35.24	35.03
October	378.9	374.5	125.76	123.12	35.84	36.82	35.36	35.16
November	381.1	376.9	125.43	123.65	35.53	36.59	35.45	35.26
December	383.3	379.2	125.89	123.74	35.72	36.62	35.75	35.41
January 1990	385.2	380.7	126.14	122.96	35.88	36.43	35.66	35.46
February	387.4	382.2	126.35	122.15	36.17	36.27	35.87	35.62
March	389.6	384.1	126.12	122.36	35.93	36.65	36.02	35.53
April	390.9	386.4	125.56	122.95	35.76	35.85	36.05	35.63
May	391.3	388.8	124.85	122.98	35.49	35.87	36.01	35.81
June	391.7	391.0	125.18	123.15	34.64	35.82	35.99	35.73

	Business Inventories		Defense Shipments		Industrial Production		Capacity Utilization	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	759.8	759.8	8.73	8.73	140.8	140.8	84.3	84.3
February	763.6	763.1	8.40	8.40	140.4	140.5	83.9	83.9
March	765.6	765.5	8.50	8.45	140.5	140.7	83.7	83.8
April	772.3	771.3	8.58	8.63	140.9	141.6	83.8	84.1
May	779.6	778.1	8.62	8.70	141.2	141.4	83.9	83.8
June	786.8	780.8	8.62	9.20	141.5	141.1	84.0	83.5
July	789.9	784.1*	8.55	9.03*	142.7	141.5*	84.4	83.6*
August	793.0	788.2	8.61	8.86	143.9	141.8	84.8	83.6
September	795.9	791.6	8.67	8.91	145.1	142.1	85.2	83.6
October	801.4	795.5	8.62	8.95	144.7	142.4	84.7	83.6
November	808.9	799.7	8.70	8.79	144.3	143.2	84.3	83.9
December	816.3	803.6	8.78	8.94	144.6	143.3	84.4	83.7
January 1990	819.4	807.5	8.68	9.01	144.5	143.4	84.1	83.5
February	822.0	811.1	8.76	9.05	144.2	143.2	83.8	83.0
March	824.6	816.1	8.90	9.09	143.9	143.3	83.5	82.9
April	828.5	820.4	8.74	9.03	143.4	143.8	83.1	83.1
May	832.4	825.5	8.67	9.10	142.9	144.4	82.7	83.3
June	833.2	830.8	8.60	9.16	142.5	144.6	82.4	83.3

Fore. = May Forecast
C.E. = Current Expectations
* = This item and those beyond it are expectations.

PRICES

	CPI-U (seasonally adjusted)		PPI Finished Goods (seasonally adjusted)		PPI-Industrial Commodities (unadjusted)		Estimated GNP Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	121.4	121.4	111.0	111.0	109.1	109.1	125.0	124.4
February	121.9	121.9	112.1	112.1	110.0	110.0	125.2	124.5
March	122.5	122.5	112.6	112.6	110.6	110.6	125.5	124.7
April	123.4	123.3	113.1	113.1	111.3	111.3	126.1	125.5
May	124.1	124.0	113.8	114.1	112.0	111.7	126.8	126.1
June	124.5	124.2	114.2	113.9	112.7	111.6	127.2	126.4
July	125.1	124.4*	114.4	113.4	113.0	111.3	127.5	126.5
August	125.6	124.6	114.7	113.4*	113.5	111.7*	127.9	126.9
September	126.2	125.0	114.7	114.4	112.5	111.6	128.3	127.3
October	126.7	125.4	115.0	114.8	113.9	112.8	128.8	127.8
November	127.2	125.9	115.3	115.3	114.0	113.3	129.3	128.3
December	127.8	126.4	115.6	115.8	114.2	113.7	129.8	128.8
January 1990	128.2	126.9	116.0	116.2	114.8	114.1	130.4	129.4
February	128.5	127.3	116.5	116.5	115.6	114.5	131.0	129.8
March	128.9	127.8	116.8	116.9	116.4	115.0	131.6	130.3
April	129.5	128.4	117.2	117.2	116.8	115.5	132.1	130.8
May	130.2	128.9	117.6	117.6	117.1	115.9	132.7	131.3
June	130.9	129.3	118.1	117.9	117.4	116.3	133.3	131.9

	Consumption Deflator		Consumer Durables		Consumer Nondurables		Consumer Services		Implicit Construction Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	127.9	127.7	112.0	111.7	119.4	118.5	138.9	137.9	116.4	118.6
February	128.1	127.9	111.7	111.3	119.5	119.7	139.2	138.9	116.6	119.8
March	128.9	128.6	111.3	110.7	121.0	121.0	139.9	139.5	116.7	120.4
April	129.6	129.4	111.6	111.0	122.2	122.8	140.5	140.0	116.9	120.5
May	130.2	129.9	111.8	110.9	123.2	123.6	141.1	140.4	117.1	120.8
June	130.8	130.1	112.0	111.1	123.6	123.4	141.7	140.8	117.3	121.0
July	131.3	130.2*	112.4	111.3*	123.8	123.2*	142.3	141.2*	117.6	121.3*
August	131.7	130.6	112.7	111.5	124.0	123.4	142.9	141.7	117.8	121.6
September	132.1	131.0	113.0	111.7	124.2	123.7	143.5	142.2	118.0	122.0
October	132.7	131.4	113.2	111.8	124.8	124.1	144.2	142.7	118.2	122.4
November	133.3	131.9	113.4	112.1	125.3	124.5	144.9	143.3	118.4	122.8
December	133.9	132.4	113.4	112.3	125.9	124.9	145.6	143.9	118.6	123.1
January 1990	134.4	132.9	113.7	112.4	126.3	125.4	146.2	144.5	118.8	123.5
February	134.8	133.3	114.0	112.6	126.6	125.8	146.9	145.0	119.0	123.9
March	135.3	133.8	114.3	112.8	127.0	126.2	147.5	145.6	119.3	124.4
April	135.9	134.3	114.4	113.0	127.7	126.6	148.3	146.2	119.5	124.9
May	136.6	134.8	114.5	113.3	128.4	127.0	149.0	146.8	119.8	125.3
June	137.2	135.3	114.4	113.5	129.0	127.5	149.7	147.5	120.0	125.8

Fore. = May Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

MISCELLANEOUS

	Merchandise Trade Balance		Leading Indicators	Estimated GNP		Estimated GNP (1982 $)		IVA (annual rate)	
	Fore.	C.E.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	-8.68	-8.90	146.1	5109	5102	4087	4101	-26.7	-31.7
February	-9.82	-9.38	145.7	5114	5111	4085	4105	-39.6	-41.6
March	-8.86	-9.48	144.7	5127	5126	4085	4111	-41.7	-49.1
April	-9.73	-8 29	145.6	5163	5176	4094	4124	-40.2	-35.3
May	-9.92	-10.24	143.7	5197	5199	4099	4123	-28.6	-18.4
June	-9.42	-10.00	143.5	5231	5210	4112	4122	-23.5	-15.3
July	-10.21	-9.53	144.1*	5256	5236	4122	4139	-25.5	-10.6
August	-10.88	-9.76	144.3	5288	5262	4134	4147	-28.0	- 3.4
September	-10.83	-9.62	143.9	5320	5290	4147	4156	-29.9	- 6.8
October	-10.62	-9.47	144.3	5341	5319	4147	4162	-28.6	-10.3
November	-10.25	-9.55	143.7	5359	5349	4145	4169	-27.4	-11.5
December	-9.56	-9.46	144.0	5379	5374	4147	4172	-26.3	-13.4
January 1990	-9.93	-9.32	143.9	5405	5403	4145	4175	-30.2	-18.1
February	-10.58	-9.23	144.2	5442	5428	4154	4182	-32.4	-18.3
March	-10.86	-9.26	144.7	5480	5451	4164	4183	-34.6	-16.7
April	-9.85	-8.95	145.0	5493	5478	4158	4188	-31.1	-19.5
May	-9.52	-8.65	144.8	5502	5506	4146	4193	-29.9	-23.8
June	-9.37	-8.56	145.0	5508	5532	4132	4194	-28.7	-27.4

	Currency Index		Adjusted Profits		30-Year Government Bonds		New York Composite	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	95.12	95.12	210.5	193.6	8.93	8.93	160.40	160.40
February	95.77	95.77	163.4	163.9	9.01	9.01	165.08	165.08
March	96.99	96.99	156.5	157.3	9.17	9.17	164.60	164.60
April	97.23	97.24	165.9	166.8	9.32	9.03	165.13	170.34
May	97.95	100.81	178.2	174.7	9.40	8.83	166.29	175.56
June	98.56	103.09	180.3	173.2	9.36	8.28	164.21	180.90
July	97.43	98.76	177.4	175.8	9.30	8.08	156.82	188.62
August	95.82	96.24*	175.7	169.6	9.25	8.09*	153.54	191.11*
September	94.16	97.62	174.0	172.2	9.21	7.93	150.26	194.43
October	93.09	95.43	173.1	170.4	9.18	8.11	148.29	186.57
November	91.70	93.48	172.4	171.2	9.12	7.89	148.86	188.77
December	90.36	94.12	171.9	168.3	9.15	7.75	149.30	184.49
January 1990	91.25	94.55	169.8	165.1	9.06	7.82	145.14	180.64
February	94.46	95.83	169.1	160.6	9.01	7.84	140.53	177.56
March	94.05	95.64	168.2	158.3	8.92	7.65	138.27	180.24
April	91.02	93.26	168.5	167.2	8.78	7.63	139.45	184.53
May	89.63	93.85	166.1	171.3	8.73	7.55	140.25	189.23
June	88.26	92.66	163.7	169.8	8.70	7.63	141.06	182.10

Fore. = May Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

FINANCIAL MARKETS

	Monetary Base		M1		M2		Federal Funds		T-Bills (6 Mos.)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	287.9	287.9	786.3	786.3	3065.9	3065.7	9.12	9.12	8.36	8.36
February	287.5	287.5	787.4	787.4	3069.7	3069.2	9.36	9.36	8.55	8.55
March	289.4	289.3	786.3	786.3	3079.5	3078.7	9.85	9.85	8.85	8.85
April	290.3	289.1	782.9	783.1	3090.4	3081.1	9.84	9.84	8.65	8.65
May	292.9	289.0	785.3	773.3	3101.3	3071.8	9.83	9.81	8.74	8.39
June	295.5	289.6	787.2	770.5	3112.2	3087.3	9.83	9.47	8.83	8.04
July	297.3	290.7*	792.5	777.2	3134.6	3119.1	10.20	9.24	8.89	7.61
August	298.1	292.1	798.9	776.8*	3158.6	3135.3*	10.23	8.96*	8.86	7.96*
September	298.9	293.6	804.9	779.8	3182.5	3151.4	10.26	8.88	8.83	7.71
October	300.4	295.2	808.6	784.2	3195.6	3169.2	10.32	8.73	8.81	7.65
November	302.8	297.0	812.4	788.6	3213.2	3187.0	10.29	8.52	8.82	7.43
December	305.2	298.3	816.2	793.0	3231.0	3205.2	10.26	8.59	8.80	7.49
January 1990	306.9	299.9	821.7	797.2	3250.4	3222.6	10.01	8.57	8.73	7.43
February	307.8	300.8	828.6	801.2	3270.3	3238.8	9.96	8.40	8.62	7.15
March	308.7	302.1	835.4	804.0	3290.1	3255.1	9.84	8.21	8.51	7.06
April	310.5	304.0	840.3	807.7	3314.3	3271.2	9.56	8.16	8.47	7.09
May	312.5	305.7	845.0	811.2	3326.1	3286.9	9.55	8.13	8.41	7.07
June	314.4	307.5	849.8	815.4	3338.0	3304.6	9.56	8.15	8.36	7.04

	Aaa (Seasoned)		Municipals (Bond Buyer)		(3 Month) Commercial Paper		90 Day CD's		Prime Rate	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
January 1989	9.62	9.62	7.35	7.35	9.04	9.04	9.20	9.20	10.50	10.50
February	9.64	9.64	7.44	7.44	9.37	9.37	9.51	9.51	10.93	10.93
March	9.80	9.80	7.59	7.59	9.95	9.95	10.09	10.09	11.50	11.50
April	9.79	9.79	7.49	7.49	9.81	9.81	9.94	9.94	11.50	11.50
May	9.75	9.57	7.45	7.25	9.80	9.47	9.93	9.59	11.50	11.50
June	9.83	9.20	7.51	7.03	9.86	9.12	9.97	9.32	11.50	11.07
July	9.89	8.93	7.58	6.96	10.17	8.68	10.26	8.76	11.68	10.98
August	9.95	8.89*	7.64	6.95*	10.26	8.66*	10.35	8.78*	12.00	10.50*
September	9.99	8.74	7.68	6.86	10.23	8.65	10.30	8.75	12.00	10.50
October	9.90	8.93	7.62	7.01	10.30	8.69	10.41	8.81	12.00	10.50
November	9.83	8.86	7.53	6.97	10.25	8.53	10.37	8.67	12.00	10.50
December	9.76	8.73	7.47	6.91	10.22	8.48	10.33	8.59	12.00	10.50
January 1990	9.70	8.76	7.40	6.87	10.07	8.43	10.22	8.56	12.00	10.50
February	9.67	8.79	7.38	6.88	9.98	8.28	10.09	8.37	11.96	10.26
March	9.64	8.62	7.35	6.75	9.88	8.04	10.05	8.19	11.50	10.00
April	9.56	8.53	7.26	6.69	9.59	8.11	9.76	8.21	11.50	10.00
May	9.53	8.59	7.20	6.70	9.53	8.17	9.71	8.29	11.28	10.00
June	9.50	8.63	7.18	6.73	9.50	8.21	9.65	8.34	11.00	10.00

Fore. = May Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

ECONOMIC FORECASTING CENTER

MONTHLY PROJECTIONS
August 1989

Dr. Donald Ratajczak, Director
For Release: Wednesday September 20, 1989

ENERGY DEFLATION AIDS ECONOMY IN THIRD QUARTER

After rising 16% during the first half of 1989, energy prices are now falling at an 8% annual rate during the third quarter. As a result of this moderation, the consumer price index should increase at less than a 3% annual rate in the quarter, while the PPI will actually decline. Although inflation excluding the energy component remains remarkably stable at slightly more than 4%, the decline in energy prices and the return to more moderate food prices is greatly increasing the difficulty of interpreting current economic conditions.

For example, the sluggish growth in real consumer expenditures during the first half can be attributed to the loss of purchasing power from a reduction in deferred income contributions that led to higher taxes in April. Also, with consumer prices expanding 6% and wages growing 4%, the capacity to engage in increased spending programs was significantly compromised. As energy prices declined in the second half and as food prices grew more slowly, the CPI was expected to slow to a gain of only 3% while wages would remain in the 4-4.5% growth range. With no significant tax drains, a surge in consumer spending should be expected.

In fact, retailers have seen some improvement in their sales activity. Back-to-school sales were reported as satisfactory and cautious increases in Christmas ordering appear to be taking place. However, the retail sales figures do not appear to confirm this rebound in consumer spending. Excluding autos, retail sales increased only 0.2% in August. (Certainly, the decline in sales of general merchandisers appears at odds with the increase in sales at apparel and hardware stores and the perceptions that sales were strong late in August. Perhaps, this portion of the retail sales report will be revised upward when September data are released.) Most analysts interpreted that report as a continuation of sluggish consumer spending. However, retail prices in August apparently fell 0.2%. Thus, annualized and adjusted for inflation, consumer spending in August grew a quite acceptable 4-4.5%. Indeed, consumer spending should grow more than 4% for the summer quarter. Coupled with further modest improvement in trade balances, moderate increases in inventories and the absence of further declines in construction, that should translate into real GNP gains of 3%.

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Of course, declining oil prices are not expected to last too much longer. Normally, gasoline prices rise during the summer and decline in the fall. However, many jobbers assumed that the OPEC productions agreements would not hold and had held low inventories of oil and product going into the spring. The Valdez oil spill changed their assessment of oil prices, leading to a surge in inventory rebuilding that generated higher oil prices sooner than normal. Gasoline prices also rose earlier than normal. When the driving season arrived, gasoline prices already had increased more than seasonal demand would have justified. The resulting glut of oil and product as demand slowed caused prices to tumble in the summer. However, as the heating season approaches, inventories again are being accumulated. The result is a gradual rise in oil prices. The result has been some firming in oil prices. As a result, the traditional decline in gasoline prices at the end of the summer driving season may be small. Currently, we are projecting that energy prices will increase 5% during the fall and rise at a 7% annual rate through much of 1990.

When gasoline prices firm, consumer spending should grow more slowly. Also, automobile prices are rising sharply for 1990 models. This has caused consumers to shift purchases to the 1989 models remaining in stock. As those stocks are depleted, auto sales are falling. This weakness will have little impact upon economic activity during the fourth quarter, as producers will be increasing their lots with the new cars. When that is accomplished however, the sluggish sales will lead to production corrections early in 1990. That weakness, in turn, should lead to rising unemployment.

Unfortunately, energy prices will be rising early in 1990, so prices and unemployment should be rising simultaneously. Fortunately, the inflation moderation currently developing should continue to restrain wage gains. As a result, underlying inflation should remain in the 4-4.5% range that has prevailed for several years. Nevertheless, the inflationary moderation that currently is developing because of falling energy prices will have ended. That will also mean that consumer sluggishness could resurface at that time.

To avoid potential recessionary behavior, the Federal Reserve is expected to ease short-term interest rates early next year. Some sympathetic downward move in long-term rates also is expected. Enough stimulus in the interest-sensitive portions of the economy is expected to insure that activity will continue to expand during the second half of next year. Of course, if the Federal Reserve persists in maintaining current interest rates early next year, an economic downturn could develop. In either case, interest rates will decline, although they will fall later and further in the recession scenario.

What should prevent a recession from developing aside from interest rate declines will be some moderate declines in the dollar's value. Thus far, relatively restrictive monetary policy in the United States has increased the attractiveness of dollar based assets. Although the interest rate differential certainly was a factor, expected changes in currency values appears to have been more important. As long as foreign investors could assume that the Federal Reserve would remain relatively restrictive, they could expect further increases in the dollar's value. With higher interest rates and an appreciating dollar, foreigners continued to be attracted to American assets. However, any signs of Federal Reserve ease or relative tightening of monetary conditions in other countries would alter that assessment. Already, European countries are defending their currency values by restricting monetary expansion. These restrictions are beginning to influence the relative attractiveness of those currencies against the yen. As a result, the surge in the dollar's value has stalled.

Any hints of Federal Reserve weakening would bring the dollar down. Such hints remain elusive but should intensify by the end of this year. Thus, the falling dollar may again encourage the growth of foreign markets as long as tight monetary policy does not shrink the size of those markets.

In addition to a rebound in trade following some dollar weakness late this year and early next year, strong spending on capital goods should continue to encourage economic expansion. Order backlogs continue to grow, suggesting that shipments will continue trending upward into the early months of next year. Thus, only a substantial plunge in consumer spending would lead to recession early in 1990. Such a plunge cannot be completely ruled out. However, the degree of consumer spending restraint currently expected should not be sufficient to spawn a recession.

Quarterly Profile of GNP

	1989-2	1989-3	1989-4	1990-1	1990-2	1990-3	1989 Annual	1990 Annual
Real:	2.7	2.8	2.3	1.3	1.4	1.4	2.9	1.7
Price:	4.6	2.9	3.8	4.1	4.7	4.7	3.9	4.3
Nominal:	7.3	5.8	6.3	5.6	6.3	6.2	7.0	6.1

Monthly Statistical Highlights

	Aug 1989	Sept 1989	Oct. 1989
Payroll Employment		+316,000	+172,000
Index of Hours Worked		+0.3%	+0.1%
Household Employment		+347,000	+208,000
Civilian Unemployment Rate		5.2%	5.1%
Personal Income	+0.2%	+0.7%	+0.5%
Savings Rate	5.0%	5.5%	5.6%
Personal Consumption	+0.9%	+0.2%	+0.4%
Retail Sales		+0.4%	+0.0%
Auto Sales		10.9*	9.6*
Housing Starts		+2.8%	+0.4%
Housing Permits		-2.9%	-0.2%
Construction Expenditures	+0.4%	+0.2%	+0.1%
Business Inventories	+0.5%	+0.5%	+0.5%
Orders for Durable Goods	+0.4%	+0.4	-0.7%
Orders - Nondefense Capital Goods	-1.5%	-0.6%	-1.7%
Industrial Production		+0.2%	+0.2%
CPI		+0.4%	+0.3%
PPI		+0.5%	+0.4%
Consumption Deflator	+0.1%	+0.3%	+0.3%
Leading Indicators	+0.6%	+0.1%	-0.2%
Currency Index		+1.0%	-1.2%
Equity Index		-4.0%	-2.4%
Real GNP (annual rate)	+2.3%	+0.6%	+2.3%
M1 (annual rate)		-9.3%	+4.0%
M2 (annual rate)		+5.0%	+6.7%

* auto sales in millions

COMMENTARY

EMPLOYMENT - Although payrolls increased by only 110,000 in August, strikes reduced payrolls by 108,000. Most of those strikes have been resolved. Therefore, a sharp increase in payroll employment is expected next month. The workweek returned to its June levels in August, suggesting that the July increase in hours worked was a fluke. Similarly, some of the increase in July's hourly earnings also may be statistical noise. Weakness in electrical equipment suggests that further softness in durable goods orders could develop in the next few months. Because most of the strike activity was in communications, little change in industrial activity was expected from this moderation in payroll growth.

It should be noted that household employment, which is not effected by strike activity, increased only 138,000. However, this series of employment is notoriously inaccurate on a monthly basis.

PERSONAL INCOME AND OUTLAYS - Although strikes should have little impact upon economic activity, they will reduce wage and salary growth in August. This should reduce savings in the month. Also, auto sales remain strong as a result of consumer shifting from higher priced cars later in the year. This means that auto sales will soar and slump. Already, those manufacturers running out of 1989 model cars have experienced deep sales declines early in September. Because prices are substantially higher for the new automobiles, expenditures will not fall as sharply as units. However, the August strike and auto sales surge should lower savings in that month. The savings rate then should gradually rebound in the next few months.

Weakness in nondurable retail sales does not conform to evidence that back-to-school sales were satisfactory. However, nondurable prices almost certainly fell in that month, suggesting that unit sales were not that sluggish. The discretionary consumer items in durables all showed substantial gains. As a result, consumer wariness is not obvious from the retail sales report. Because of price weakness, consumer spending is expected to grow strongly in August after adjustment for inflation.

Farm income typically reaches its low point prior to the new harvest. However, incomes already have fallen so far that some rebound should be expected. Coupled with increased property income, these gains should permit modest increases in personal income for August.

CONSTRUCTION - Recently, housing starts have been anticipated by housing permits in the previous month. Thus, the August decline in housing starts was apparent from the July collapse in permits for apartment units. Also, July's starts probably included some catch-up from the poor weather in June. August permits suggest that some modest rebound should be expected in September starts for single and multiple units. However, the stall in interest rates probably will prevent any further significant rebound in housing activity until next year.

A rebound is expected in public construction and in housing expenditures in August, as suggested by the increase in hours worked. Further modest increases in construction activity are expected for the remainder of this year and in 1990. The construction cost index is rising slightly less than 4% per year and should continue to do so in this moderate construction climate.

BUSINESS ACTIVITY - Business inventories rose a strong 0.6% in July as manufacturing and retail inventories advanced. Retail inventories should fall slightly in August and September as auto stocks are depleted. However, the drop in commodity prices means that the IVA is hardly increasing. This means that the quality of profits is improving rapidly, but it also means that nearly all of the inventory increase is in units rather than prices. Thus, inventory investments during the third quarter could be larger than in the spring. Although a dip in sales led to a high inventory-sales ratio, strong sales relative to production in August and September should eliminate any serious inventory overhang at this time.

Manufacturing shipments and orders were surprisingly weak in July, as defense orders and shipments fell and electrical equipment orders continued to contract. However, orders for nondefense capital goods continued to grow. Excluding aircraft, orders remained well above shipments, suggesting a rebound in shipments in the fall.

Industrial production was revised upward sharply in June, suggesting that second quarter GNP could be revised further upward. As auto assemblies were a sluggish 6.3 million in August and utility output fell in that month, further increases in industrial activity should be expected through the fall. This means that capacity utilization will remain high. However, capacity has finally begun to accelerate according to the latest report. This should prevent any serious inflationary pressures in most industries in the months ahead.

PRICES - Plunging energy prices are restraining price increases for all the major indices during the summer months. Indeed, the GNP deflator probably will increase less than 3% during the summer. Consumer prices certainly are growing less than 2% while the PPI is actually falling. However, these are price declines that were expected to occur more slowly. Thus, our longer term projections are not altered by the timing of these price declines.

There is some favorable impact from these price declines, however. Many contracts remain tied directly or indirectly to the CPI. Therefore, wage gains will be more moderate in the fall and early next year because of this period of price moderation. Also, the July surge in service inflation was related to small service categories whose prices change only infrequently. Thus, claims that service inflation was intensifying are not justified by this report.

MISCELLANEOUS - Flat prices and rising permits suggest that the leading indicators will rise sharply this month. Also adding to the indicators are initial claims, stock prices and an anticipated rebound in consumer orders. Sensitive prices are beginning to rebound following several weak months, while delivery delays also seem to have increased.

With a sharp decline both in exports and imports, the trade report appears to have been compiled with several days worth of data missing. If so, exports, imports, and the deficit should rebound next month. Certainly, the decline in exports is troubling and may begin to reflect reduced competitiveness from the strengthening dollar. The composition of imports was appropriate for the domestic economy, which is experiencing a rebound in consumer spending and some caution in capital goods purchases. However, capital goods imports should again rebound later in the year. Thus, trade deficits are expected to deteriorate in the next few months.

Little change in interest rates but rising trade deficits may gradually undermine the dollar's strength. Although dollar weakness could become dramatic once any weakness develops, our current estimates suggest that differential interest rates will remain sufficiently strong to prevent any wholesale dollar decline.

Because of the decline in commodity prices, the inventory valuation adjustment (IVA) is expected to be smaller than previously expected. This significantly raises the quality of corporate earnings. Nevertheless, slower economic growth next year should reduce profits while little change in interest rates should undermine stock market values in the next few months. A rebound in the market is expected by midyear and the sell-off should not be substantial, but a modest sell-off is expected.

FINANCIAL MARKETS

A surge in durable goods purchases and a reduction in wage gains from strike activity has caused a decrease in household net savings during the summer months. Modest gains in housing activity could generate some mortgage investment in the fall. Further housing gains are expected early next year. As a result, the household sector has reduced its support to the credit markets in the summer and should only modestly add to net savings early next year.

Following the surge in tax collections during the spring, the federal government has been trying to prevent a surge in borrowings through the summer. However, the thrift bailout bill requires the acquisition of more than $20 billion of deposit support before the end of the current fiscal year. This means that federal deficits are rising significantly at this time. To be sure, most of the thrift bailout results in a portfolio shift, as federal funds replace deposits in support of assets. The interest rate pressures were incurred when those assets were accumulated. Nevertheless, the portfolio shifts lead to declines in checkable deposits and to the substitution of long-lived liabilities for short-term liabilities. This should result in a slightly steeper yield curve than otherwise would have developed. Also, the increased government borrowings as tax collections fall off should increase interest rate pressures.

Corporate borrowings intensified early in the third quarter, as inventories grew and operating profits were squeezed. However, the decline in commodity prices has eased the financing of inventories while strong consumer spending has increased operating profits. Therefore, the corporate sector has been able to supply more funds to credit markets late in the quarter. Later in the year, rising commodity prices and rising auto inventories could again put upward pressures upon interest rates. Then inventory reductions early next year should lead to reduced interest rate pressures.

Of course, foreign investors remain attracted to American assets. Therefore, the shift in government borrowings has been offset by increased demand for American assets by foreigners. However, a falling dollar late this year could reduce foreign support. As a result, some rising interest rate pressures could develop. However, the weakness in corporate borrowings early in 1990 should more than offset the foreign impact. Thus, some modest declines in interest rates are expected at that time. Interest rates then are expected to stabilize during the second half of next year at lower rates than currently prevail.

EQUITY MARKETS - Once every few months, the stock market is susceptible to "whistling in the dark." According to our analysis, the market currently commands a premium for the asset value of potential takeover candidates. However, those asset values are based upon financing arrangements that recently have priced some assets so highly that cash flow did not cover current interest rate requirements. Asset sales or balloon (or in-kind) interest rates were needed to make the deal. But growth tends to slow after corporate restructurings, leading to reduced ability to finance those deals. This overpricing of assets has become more apparent as the newly created junk bonds have become more suspect. Except in the airlines, the stock market appears to have ignored this new truth in asset values. For this reason, a stock market correction is expected in the next few weeks.

However, any correction should be limited as the quality of earnings is again improving and strong sales growth should add to operating profits late this year. Our current projections suggest the correction will be about 12% over the next six months.

Of course, those companies without inflated asset values should benefit from improved operating profits and could actually experience some gains in stock market values even as the correction is developing. Some interest sensitive and building material based industries could perform well. Utilities appear to have better than average opportunities for advancement. New products at the November Comdex association could re-ignite interest in the technology issues. Some of the nonferrous metals producers also should perform well, although precious metals still appear to be in a downdraft.

On balance, stock profits should be taken, especially in those takeover possibilities. Some increase in bond holdings may be appropriate, although the especially narrow spreads between agencies and government securities suggest that treasuries could be more beneficial. The spreads on high yield bonds have climbed to nearly 6%, which should compensate for more than 3% annual defaults in such portfolios. In the absence of recession, this spread should be adequate for investing in higher quality junk bonds. However, coupons in excess of 15% should be shunned, as such interest rate commitments exceed the normal expectations of earnings on capital. Without a significant equity base to support such bonds, defaults are likely. In short, the markets are generating substantial opportunities, but investors must now be selectively rather than buy the market.

EMPLOYMENT

	Payroll Employment		Index of Hours Worked		Household Civilian Employment		Civilian Unemployment Rate		Hourly Earnings	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	108101	108101	128.7	128.7	117113	117113	5.3	5.3	9.61	9.61
May	108310	108310	127.6	127.6	117215	117215	5.2	5.2	9.60	9.60
June	108560	108607	128.0	128.1	117541	117541	5.3	5.3	9.62	9.62
July	108793	108791	128.4	129.2	117743	117459	5.2	5.2	9.68	9.70
August	108884	108901	128.7	128.5	117929	117597	5.2	5.2	9.72	9.69
September	109125	109217*	129.0	128.9*	118115	117844*	5.1	5.2*	9.77	9.73*
October	109316	109389	129.1	129.0	118328	118052	5.1	5.1	9.81	9.77
November	109506	109578	129.3	129.2	118524	118240	5.1	5.2	9.85	9.82
December	109698	109805	129.5	129.4	118720	118467	5.1	5.1	9.88	9.85
January 1990	109843	109994	129.7	129.6	118896	118708	5.2	5.1	9.94	9.88
February	110015	110107	129.6	129.6	119046	118829	5.2	5.2	9.98	9.92
March	110187	110210	129.7	129.7	119195	118964	5.1	5.3	10.02	9.95
April	110326	110391	130.0	130.0	119353	119163	5.1	5.3	10.06	9.99
May	110469	110562	130.2	130.2	119517	119336	5.1	5.3	10.11	10.03
June	110615	110743	130.5	130.4	119668	119494	5.2	5.4	10.16	10.07
July	110736	110916	130.4	130.5	119814	119692	5.2	5.4	10.20	10.11
August	110881	111104	130.5	130.8	119966	119879	5.2	5.4	10.24	10.16
September	111026	111288	130.7	131.0	120118	120100	5.2	5.3	10.29	10.21

PERSONAL INCOME

	Personal Income		Wage & Salary		Personal Savings		Disposable Income		Personal Outlays	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	4.387	4.387	2.601	2.601	183.3	182.3	3.718	3.718	3.535	3.536
May	4.395	4.396	2.604	2.604	203.5	193.4	3.747	3.747	3.543	3.553
June	4.407	4.416	2.617	2.621	224.1	215.8	3.769	3.776	3.545	3.560
July	4.435	4.449	2.640	2.647	225.0	217.7	3.795	3.804	3.570	3.587
August	4.458	4.458*	2.651	2.644*	226.3	191.8*	3.813	3.810*	3.587	3.618*
September	4.481	4.489	2.662	2.663	224.1	210.6	3.831	3.836	3.607	3.625
October	4.503	4.513	2.680	2.676	234.6	215.9	3.850	3.855	3.615	3.639
November	4.527	4.531	2.698	2.695	232.7	209.6	3.871	3.868	3.638	3.658
December	4.551	4.553	2.716	2.708	230.8	208.1	3.892	3.885	3.661	3.677
January 1990	4.575	4.572	2.730	2.722	232.4	214.5	3.911	3.907	3.679	3.693
February	4.602	4.594	2.745	2:734	234.0	213.0	3.932	3.926	3.698	3.713
March	4.629	4.617	2.760	2.746	233.2	209.1	3.953	3.945	3.720	3.736
April	4.649	4.646	2.776	2.764	223.4	209.1	3.970	3.958	3.747	3.749
May	4.672	4.673	2.794	2.781	216.0	221.4	3.983	3.989	3.767	3.768
June	4.695	4.700	2.812	2.797	224.5	228.3	3.996	4.010	3.771	3.782
July	4.710	4.724	2.825	2.812	230.3	223.9	4.020	4.027	3.790	3.803
August	4.729	4.764	2.838	2.832	231.7	239.7	4.045	4.064	3.813	3.824
September	4.749	4.791	2.851	2.851	233.1	244.0	4.070	4.086	3.837	3.842

Fore. = August Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

CONSUMPTION

	Personal Consumption		Durables		Nondurables		Services		Consumption Real	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	3433.2	3433.5	477.3	477.2	1113.2	1112.9	1841.7	1843.4	2652.5	2653.3
May	3440.2	3450.2	467.7	466.6	1118.1	1126.7	1854.4	1856.9	2647.8	2655.5
June	3441.4	3456.8	466.0	469.2	1118.5	1126.5	1856.9	1861.1	2644.3	2657.2
July	3468.2	3482.2	468.5	476.8	1126.4	1131.1	1873.3	1874.3	2657.6	2670.6
August	3483.4	3513.5*	470.1	490.0*	1128.7	1137.3*	1884.6	1886.2*	2663.2	2690.9*
September	3495.9	3520.3	468.9	480.9	1131.1	1141.8	1895.9	1897.6	2666.6	2687.4
October	3509.8	3533.5	465.0	477.7	1136.5	1146.7	1908.3	1909.1	2667.0	2689.3
November	3531.3	3552.4	467.0	479.6	1142.3	1152.1	1922.0	1920.7	2671.2	2694.9
December	3552.8	3570.4	469.0	481.7	1148.1	1157.3	1935.7	1931.4	2675.3	2698.6
January 1990	3571.6	3585.1	469.7	479.7	1154.1	1162.5	1947.8	1942.9	2679.4	2699.3
February	3590.1	3605.2	471.2	482.9	1159.3	1167.7	1959.6	1954.6	2685.2	2704.3
March	3608.8	3627.7	472.9	488.1	1164.5	1172.4	1971.4	1967.2	2691.1	2710.6
April	3631.7	3640.3	477.2	484.8	1170.2	1177.0	1984.3	1978.5	2698.1	2709.8
May	3653.2	3658.6	478.6	486.6	1176.4	1181.2	1998.2	1990.8	2702.1	2712.7
June	3676.0	3672.7	481.3	484.4	1182.6	1185.5	2012.1	2002.8	2706.9	2712.4
July	3685.4	3693.6	473.9	488.5	1187.3	1190.5	2024.2	2014.6	2703.9	2717.8
August	3702.1	3714.3	473.7	492.2	1192.4	1195.5	2036.0	2026.6	2708.2	2723.5
September	3722.1	3731.0	477.0	491.7	1197.3	1200.2	2047.8	2039.1	2712.9	2724.9

RETAIL SALES

	Retail Sales		Non-Auto Durables		Auto (Million Units)		Nondurable Sales		Auto Sales	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	141.07	140.94	22.41	22.41	10.8	10.8	87.30	87.12	31.36	31.41
May	142.10	142.54	22.97	22.97	10.2	10.1	88.20	88.40	30.93	31.17
June	142.17	142.50	22.79	22.85	10.0	9.9	88.66	88.48	30.72	31.17
July	142.49	143.27	22.84	22.75	10.0	10.2	88.83	88.83	30.82	31.69
August	142.85	144.29	22.70	23.26	10.6	11.5	89.01	88.52	31.14	32.50
September	142.91	144.82*	22.71	23.03*	10.6	10.9*	89.20	89.74*	31.00	32.05*
October	142.88	144.84	22.80	23.12	9.4	9.6	89.62	90.13	30.46	31.59
November	143.57	145.48	22.88	23.16	9.7	9.7	90.08	90.55	30.61	31.77
December	144.26	146.13	22.96	23.22	9.8	9.8	90.54	90.96	30.76	31.95
January 1990	144.81	146.31	22.90	23.08	9.7	9.7	91.01	91.37	30.90	31.86
February	145.39	147.09	22.98	23.18	9.8	9.9	91.42	91.78	30.99	32.13
March	145.99	148.05	23.04	23.24	9.9	10.2	91.83	92.15	31.12	32.66
April	146.94	148.04	23.00	23.25	10.0	10.0	92.28	92.51	31.66	32.28
May	147.59	148.57	23.07	23.38	10.0	10.0	92.77	92.84	31.75	32.35
June	148.39	148.66	23.14	23.33	10.2	9.9	93.26	93.18	31.99	32.15
July	147.91	149.52	23.02	23.44	9.7	10.1	93.63	93.57	31.26	32.51
August	148.29	150.33	23.08	23.39	9.6	10.6	94.03	93.96	31.18	32.98
September	149.05	150.65	23.15	23.48	9.7	10.5	94.42	94.33	31.48	32.84

Fore. = August forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

CONSTRUCTION

	Housing Starts		Single Family Starts		Housing Permits		Construction Expenditures (Current)		Construction Expenditures (Real)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	1.343	1.343	1.029	1.029	1.334	1.334	415.8	415.8	345.0	345.0
May	1.309	1.308	0.977	0.977	1.347	1.347	418.2	418.2	346.2	346.2
June	1.400	1.406	0.975	0.972	1.300	1.308	414.7	414.7	342.7	342.7
July	1.404	1.424	0.989	1.029	1.305	1.281	419.5	419.2	345.0	344.2
August	1.422	1.353	1.005	1.003	1.315	1.326	421.4	420.7*	344.8	344.3*
September	1.439	1.391*	1.021	1.026*	1.332	1.288*	423.8	421.6	344.8	343.9
October	1.445	1.396	1.025	1.025	1.329	1.286	426.5	422.1	346.2	343.2
November	1.461	1.372	1.021	0.996	1.345	1.277	429.8	424.6	348.6	345.2
December	1.456	1.394	1.029	1.002	1.347	1.285	433.3	424.6	350.9	343.8
January 1990	1.443	1.401	1.025	1.013	1.328	1.294	434.5	426.3	350.4	344.1
February	1.461	1.413	1.028	1.025	1.343	1.304	436.2	430.0	349.8	345.9
March	1.478	1.408	1.031	1.022	1.351	1.302	438.1	430.9	349.6	345.3
April	1.485	1.437	1.033	1.043	1.366	1.326	440.1	431.8	350.1	344.9
May	1.481	1.450	1.038	1.056	1.374	1.342	442.4	436.2	350.6	347.0
June	1.477	1.443	1.036	1.048	1.365	1.341	445.3	437.9	351.7	347.0
July	1.466	1.463	1.031	1.056	1.355	1.353	448.0	439.6	352.5	347.2
August	1.474	1.467	1.025	1.050	1.366	1.361	449.3	441.2	352.1	347.1
September	1.482	1.473	1.020	1.062	1.378	1.367	451.4	443.3	352.4	347.4

	Non-Residential		Public Construction		Residential Construction	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	131.4	131.4	80.4	80.4	204.0	204.0
May	133.3	133.1	84.7	85.1	200.2	201.0
June	136.1	135.1	80.6	81.9	197.9	198.6
July	137.0	136.5	83.0	80.9	199.5	198.2
August	136.6	135.8*	83.9	82.4*	200.9	201.0*
September	136.5	136.0	84.8	83.3	202.5	201.4
October	137.1	136.3	83.8	83.8	205.6	201.5
November	137.7	136.5	83.3	84.0	208.8	201.6
December	138.4	137.2	82.9	84.4	212.0	203.0
January 1990	138.0	137.5	83.3	84.3	213.2	204.5
February	138.8	138.1	83.7	84.8	213.7	207.1
March	139.6	138.5	84.2	85.2	214.3	207.2
April	140.0	138.2	84.0	85.5	216.1	208.1
May	139.6	138.6	84.2	86.0	218.6	211.6
June	140.2	139.0	84.1	86.3	221.0	212.6
July	140.6	139.6	85.2	86.6	222.2	213.4
August	141.6	140.3	85.0	86.9	222.7	214.0
September	142.5	140.8	85.6	87.3	223.3	215.2

Fore. = August Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

BUSINESS ACTIVITY

	Manufacturers' Inventories		Durable Goods Orders		Non-Defense Capital Goods Orders		Non-Defense Capital Shipments	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	363.5	363.5	129.37	129.37	40.39	40.39	34.60	34.60
May	365.1	365.1	123.68	123.52	37.29	37.29	34.53	34.53
June	366.2	366.5	124.19	125.14	37.39	39.15	34.59	34.76
July	369.3	370.4	125.43	122.42	36.69	41.37	34.82	34.46
August	371.3	372.7*	126.17	122.91*	36.73	40.76*	35.03	34.42*
September	373.2	374.3	125.84	123.46	36.45	40.51	35.24	34.53
October	375.3	375.9	124.76	123.12	35.64	39.82	35.06	34.16
November	377.4	377.4	124.43	123.65	35.24	40.59	34.93	34.78
December	379.5	379.0	125.89	124.74	35.82	40.62	35.12	35.03
January 1990	381.2	380.4	126.14	122.96	35.98	39.43	35.66	34.46
February	383.2	381.6	127.35	123.15	36.27	40.27	35.87	35.13
March	385.1	383.2	127.53	123.36	36.41	40.65	35.94	35.53
April	386.0	385.0	128.56	124.95	36.98	40.85	36.45	35.83
May	386.9	386.5	128.85	124.98	37.23	40.27	36.51	35.81
June	387.8	387.8	129.18	125.15	37.64	40.82	36.69	36.04
July	388.6	389.1	130.14	126.33	37.83	41.36	36.81	36.43
August	389.6	390.5	130.42	126.14	37.95	40.93	36.95	36.62
September	390.5	392.0	129.64	126.01	37.82	40.52	36.90	36.94

	Business Inventories		Defense Shipments		Industrial Production		Capacity Utilization	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	771.3	771.3	8.63	8.63	141.6	141.7	84.1	84.2
May	778.1	778.1	8.70	8.70	141.4	141.6	83.8	84.0
June	780.8	780.8	9.20	9.23	141.1	141.9	83.5	83.9
July	783.3	785.5	8.86	8.19	141.4	142.0	83.5	83.8
August	785.1	789.4*	8.94	8.56*	141.8	142.4	83.6	83.8
September	787.0	793.1	9.02	8.84	142.2	142.7*	83.7	83.8*
October	792.6	796.7	9.06	8.95	142.7	143.0	83.8	83.8
November	798.0	799.9	9.11	8.79	143.2	143.2	83.9	83.7
December	803.4	803.6	9.16	8.94	143.6	143.5	84.0	83.8
January 1990	806.5	806.7	9.12	9.01	143.1	143.8	83.3	83.8
February	809.5	809.2	9.15	9.05	142.5	144.0	82.7	83.7
March	813.6	812.8	9.19	9.09	142.5	143.7	82.4	83.3
April	817.9	817.4	9.12	9.03	143.0	143.9	82.5	83.4
May	822.2	820.9	9.07	9.10	143.6	144.2	82.6	83.4
June	825.4	823.7	9.08	9.06	144.1	144.5	82.6	83.4
July	825.8	826.5	9.16	8.93	143.3	144.2	82.2	83.0
August	826.1	829.5	9.30	8.96	142.8	144.5	82.2	83.0
September	826.5	832.7	9.45	9.02	142.9	144.9	82.1	83.1

Fore. = August Forecast
C.E. = Current Expectations
* = This item and those beyond it are expectations.

PRICES

	CPI-U (seasonally adjusted)		PPI Finished Goods (seasonally adjusted)		PPI-Industrial Commodities (unadjusted)		Estimated GNP Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	123.3	123.3	113.1	113.1	111.8	111.7	125.5	125.5
May	124.0	124.0	114.1	114.1	112.3	112.4	126.1	125.9
June	124.2	124.2	113.9	114.0	112.2	112.3	126.4	126.2
July	124.7	124.4	113.7	113.5	112.0	112.2	126.7	126.5
August	125.0	124.4	113.5	113.0	112.1	111.7	127.0	126.7
September	125.3	125.1*	114.0	113.7*	111.6	111.4*	127.5	127.1
October	125.8	125.5	114.3	114.3	112.6	112.3	128.0	127.5
November	126.2	125.9	114.6	114.8	112.9	112.8	128.5	128.0
December	126.6	126.4	114.9	115.1	113.3	113.4	129.0	128.5
January 1990	127.0	126.9	115.2	115.4	114.0	114.0	129.4	129.1
February	127.5	127.4	115.5	115.8	114.6	114.5	129.8	129.6
March	128.0	127.9	115.8	116.2	115.2	115.0	130.2	130.1
April	128.5	128.4	116.3	116.6	115.7	115.5	130.7	130.6
May	129.0	128.9	116.8	117.0	116.1	115.9	131.1	131.1
June	129.5	129.3	117.2	117.3	116.5	116.3	131.6	131.6
July	130.1	129.8	117.7	117.7	117.0	116.8	132.0	132.1
August	130.8	130.3	118.2	118.2	117.4	117.3	132.5	132.6
September	131.5	130.8	118.7	118.6	116.5	116.6	133.0	133.1

	Consumption Deflator		Consumer Durables		Consumer Nondurables		Consumer Services		Implicit Construction Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	129.4	129.4	111.0	110.9	122.8	122.8	140.0	140.0	120.5	120.5
May	129.9	129.9	110.9	110.7	123.6	123.6	140.4	140.4	120.8	120.8
June	130.1	130.1	111.1	110.9	123.4	123.5	140.8	140.8	121.0	121.0
July	130.5	130.4	111.3	111.2	123.5	123.3	141.3	141.5	121.6	121.4
August	130.8	130.6*	111.5	111.5*	123.6	123.2*	141.8	142.0*	122.2	121.8*
September	131.1	131.0	111.8	111.9	123.8	123.3	142.4	142.5	122.9	122.2
October	131.6	131.4	112.0	112.0	124.2	123.6	143.0	143.0	123.2	122.6
November	132.2	131.8	112.2	112.0	124.7	124.0	143.6	143.6	123.3	123.0
December	132.8	132.3	112.4	112.3	125.2	124.4	144.2	144.2	123.5	123.5
January 1990	133.3	132.8	112.4	112.4	125.6	124.9	144.8	144.8	124.0	123.9
February	133.7	133.3	112.6	112.6	126.0	125.4	145.4	145.4	124.7	124.3
March	134.1	133.8	112.7	112.8	126.5	126.0	146.0	146.0	125.3	124.8
April	134.6	134.3	113.0	113.0	127.1	126.4	146.6	146.6	125.7	125.2
May	135.2	134.9	113.3	113.3	127.6	126.9	147.2	147.2	126.2	125.7
June	135.8	135.4	113.5	113.5	128.0	127.4	147.8	147.8	126.6	126.2
July	136.3	135.9	113.7	113.7	128.4	127.8	148.4	148.5	127.1	126.6
August	136.7	136.4	114.0	114.0	128.7	128.2	149.0	149.1	127.6	127.1
September	137.2	136.9	114.3	114.3	129.1	128.7	149.6	149.7	128.1	127.6

Fore. = August Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

MISCELLANEOUS

	Merchandise Trade Balance		Leading Indicators	Estimated GNP		Estimated GNP (1982 $)		IVA (annual rate)	
	Fore.	C.E.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	-8.29	-8 29	145.6	5175	5186	4124	4132	-35.3	-34.9
May	-8.83	-10.08	143.7	5197	5208	4121	4137	-18.4	-18.9
June	-8.71	-8.01	143.7	5211	5217	4123	4134	-15.3	-14.3
July	-8.73	-7.58	144.0	5246	5245	4140	4146	-19.9	-10.6
August	-8.45	-8.41*	144.9*	5273	5263	4152	4154	-20.1	- 3.4
September	-8.93	-8.77	145.0	5301	5282	4158	4156	-19.2	- 5.8
October	-8.66	-9.04	144.7	5334	5309	4167	4164	-20.6	-11.3
November	-8.73	-8.55	144.3	5367	5340	4177	4172	-21.4	-13.5
December	-8.81	-8.46	144.6	5399	5368	4185	4177	-23.3	-14.4
January 1990	-8.16	-8.32	144.8	5416	5399	4185	4182	-31.1	-19.1
February	-8.05	-8.23	144.5	5428	5422	4182	4184	-30.2	-20.6
March	-7.95	-8.26	144.7	5441	5441	4179	4182	-27.6	-22.5
April	-8.16	-8.17	145.0	5477	5474	4191	4191	-21.1	-22.2
May	-8.24	-8.05	144.8	5512	5500	4204	4195	-14.9	-23.8
June	-8.36	-8.26	145.0	5547	5529	4215	4201	-16.7	-27.4
July	-8.12	-8.11	145.3	5563	5551	4214	4202	-20.6	-26.4
August	-8.28	-8.23	145.6	5582	5582	4213	4210	-25.3	-24.5
September	-8.36	-8.13	145.4	5602	5611	4212	4216	-29.9	-24.2

	Currency Index		Adjusted Profits		30-Year Government Bonds		New York Composite	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	97.24	97.24	165.9	167.8	8.89	9.03	170.34	169.38
May	100.81	100.81	176.2	178.7	8.85	8.83	175.56	175.30
June	103.09	103.09	177.3	180.3	8.46	8.27	180.90	180.76
July	98.43	99.12	178.4	185.3	8.31	8.08	188.43	185.15
August	97.12	100.44	171.7	187.9	8.22	8.12	187.72	192.83
September	95.76	101.46*	164.0	183.4	8.13	8.14*	185.43	185.10*
October	94.43	100.22	168.5	178.4	8.18	8.11	185.67	180.72
November	94.82	99.84	170.4	173.2	8.12	8.19	183.19	173.74
December	95.36	99.63	172.1	170.9	8.15	8.12	180.74	172.91
January 1990	96.25	96.72	164.8	166.2	7.81	7.93	172.25	172.18
February	95.46	95.83	160.1	162.4	7.73	7.84	165.76	170.18
March	94.86	95.64	158.2	158.7	7.68	7.85	159.50	172.24
April	93.26	96.28	165.5	164.3	7.72	7.73	158.77	178.53
May	92.94	95.88	171.2	168.2	7.66	7.75	159.38	182.30
June	92.96	98.43	171.5	171.3	7.70	7.83	163.46	183.76
July	92.15	97.24	167.3	166.2	7.68	7.78	162.53	186.42
August	91.82	95.54	161.6	168.3	7.63	7.88	165.12	188.93
September	91.56	95.42	155.8	167.9	7.69	8.07	167.83	185.56

Fore. = August forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

FINANCIAL MARKETS

	Monetary Base		M1		M2		Federal Funds		T-Bills (6 Mos.)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	289.1	289.0	783.1	783.1	3081.1	3080.6	9.84	9.84	8.65	8.65
May	289.0	289.0	773.3	773.3	3071.8	3072.1	9.81	9.81	8.39	8.39
June	289.6	289.7	770.5	770.3	3087.3	3087.9	9.47	9.53	8.04	7.93
July	290.9	290.5	777.2	777.3	3119.1	3117.2	9.23	9.24	7.89	7.61
August	293.8	290.7	783.2	777.7	3136.1	3136.0	9.11	8.99	7.63	7.74
September	296.7	291.1*	787.4	771.4*	3153.2	3148.7*	8.99	8.93*	7.70	7.8*
October	298.0	292.6	790.7	773.9	3171.6	3165.7	8.73	8.95	7.75	7.80
November	299.2	294.0	794.4	778.4	3190.3	3182.0	8.77	8.91	7.79	7.73
December	299.9	295.3	797.8	781.6	3209.0	3198.3	8.70	8.88	7.80	7.59
January 1990	301.8	296.9	800.4	787.2	3223.6	3215.6	8.33	8.67	7.42	7.43
February	303.3	298.5	803.7	790.1	3237.2	3233.8	8.13	8.43	7.38	7.22
March	304.9	300.1	807.0	794.0	3250.9	3250.6	7.94	8.26	7.34	7.26
April	306.5	302.0	813.3	797.7	3272.1	3267.4	7.87	8.26	7.19	7.19
May	307.9	303.7	818.4	801.2	3294.0	3283.9	7.83	8.23	7.15	7.17
June	309.3	305.5	823.5	805.4	3315.8	3300.6	7.80	8.25	7.11	7.04
July	311.0	306.6	828.4	807.3	3331.6	3317.5	7.76	8.02	7.01	6.97
August	312.4	308.0	831.8	810.2	3352.5	3332.8	7.73	7.99	7.00	7.03
September	314.2	309.5	835.1	814.6	3373.3	3346.9	7.79	8.03	7.06	7.12

	Aaa (Seasoned)		Municipals (Bond Buyer)		(3 Month) Commercial Paper		90 Day CD's		Prime Rate	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	9.79	9.79	7.49	7.49	9.81	9.81	9.94	9.94	11.50	11.50
May	9.57	9.57	7.25	7.25	9.47	9.47	9.59	9.59	11.50	11.50
June	9.20	9.10	7.03	7.02	9.12	9.11	9.32	9.20	11.07	11.07
July	8.99	8.94	6.85	6.96	9.17	8.68	9.35	8.76	10.83	10.98
August	8.95	8.96	6.84	7.06	9.05	8.57	9.26	8.64	10.50	10.50
September	8.90	8.93*	6.80	7.11*	8.96	8.78*	9.15	8.85*	10.50	10.50*
October	8.90	8.98	6.81	7.13	8.70	8.83	8.91	8.94	10.50	10.50
November	8.83	9.06	6.73	7.22	8.76	8.81	8.97	8.97	10.50	10.50
December	8.76	9.03	6.67	7.15	8.68	8.78	8.92	8.94	10.50	10.50
January 1990	8.63	8.76	6.55	6.97	8.26	8.53	8.52	8.68	10.03	10.50
February	8.57	8.69	7.48	6.88	8.08	8.38	8.23	8.52	9.57	10.13
March	8.43	8.72	6.35	6.93	7.88	8.22	8.05	8.39	9.50	10.00
April	8.56	8.65	6.46	6.89	7.79	8.23	7.93	8.40	9.50	10.00
May	8.63	8.67	6.54	6.90	7.85	8.17	7.99	8.33	9.50	10.00
June	8.60	8.73	6.55	6.99	7.84	8.21	7.98	8.37	9.50	10.00
July	8.46	8.76	6.41	7.04	7.71	7.94	7.89	8.14	9.50	9.79
August	8.39	8.85	6.35	7.15	7.75	7.96	7.92	8.16	9.50	9.75
September	8.50	9.02	6.49	7.34	7.82	8.08	7.97	8.22	9.50	9.75

Fore. = August forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

ECONOMIC FORECASTING CENTER

MONTHLY PROJECTIONS
September 1989

Dr. Donald Ratajczak, Director
For Release: Thursday October 26, 1989

NATURAL DISASTERS WILL GENERATE SOME INFLATION AND ECONOMIC GROWTH

Following a third quarter of strong consumer activity, moderate economic growth, and modest inflation, the economy entered the last quarter with export activity definitely losing steam and capital spending beginning to slow. Also, housing activity has not responded to the modest interest rate declines that have developed in recent weeks. As a result, some economists once again are suggesting that the next recession is just around the corner.

Certainly, consumer spending cannot sustain its vigorous third quarter growth, especially as inflation has reappeared. Also, summer auto sales were borrowed from the fourth quarter. As a result, sales are falling sharply behind production in autos and trucks during the fall. Some production curtailments almost certainly should surface by the winter. By that time, however, some moderation in the dollar's value should reignite export growth, while a sluggish fourth quarter should begin to slow import activity. Housing finally should respond to reduced interest rates and rising rental rates that a falling vacancy rate in apartments should begin to generate. While capital spending will be sluggish next year, improved technology for information and communications equipment may begin generating increased activity in that portion of investment activity by the second half of next year. Assuming payrolls will grow modestly early in the year, enough purchasing power should be generated to insure modest consumption growth through the year. Therefore, slow economic growth early in the year should gradually give way to more robust activity later in the year.

Of course, any pick-up in activity could risk higher inflationary pressures. Wages already are rising slightly and a hike in the social security tax will add to the hourly costs of wage compensation. Therefore, renewed Federal Reserve restraint late next year to prevent the inflation rate from going sharply above 5% might again create slow or no growth early in 1991. Thus, the economy is in for a bumpy ride, but the recession still appears to be more than a year away.

However, two natural events have created further distortions in economic statistics. Hurricane Hugo may have destroyed more than $5 billion of housing, highway, and productive capital. Some saw mills and an aluminum smelter were damaged, more than a billion dollars of timber was blown to the ground, and the damage and power loss was so extensive that more than 80,000 people applied for unemployment insurance

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in the Hugo area the week following the storm. Even adding the overtime payrolls of more than 5000 utility workers who converged on South Carolina from other companies throughout the southeast, nearly a quarter biliion dollars in lost wages will occur before production facilities once again are operational.

While more lives were lost and more damage was inflicted in the San Francisco earthquake, the loss of productive activity was much smaller than in South and North Carolina. Damaged public infrastructure, homes, and other real estate may generate losses in excess of $7 billion. Combined, the two natural disasters reduced the nation's wealth by more than a dozen billion dollars.

As the GNP accounts assume that housing capital is rented to homeowners by themselves and therefore generates an imputed rental value, much of the damage will reduce the production possibilities curve of the United States. In short, our ability to supply housing services will be reduced by the return on as much as $10 billion. This will be shown as a sharp drop in net rental income in the personal income accounts. The result will be a significant drop in disposable income during September and October, when the two events occurred.

However, GNP is not affected significantly by the loss of housing capital, because the destroyed property is treated as an additional depreciation. Of course, all the highway destruction has no impact upon the GNP accounts, because, as government goods, they were assumed to have been consumed when they were created. Clearly, GNP is reduced by the lost production in lodging, restaurant, manufacturing, and other activities that the two events created. However, if that cancelled vacation in San Francisco is taken somewhere else, only regional economic distortions will prevail.

Thus, while the loss of imputed rental income is substantial, possibly as much as $4 billion in the third quarter and $6 billion during the fall (which needs to be annualized), the loss of GNP should be only $1-2 billion annualized because of the lost payrolls, and nearly all of that probably occurred in the Carolinas during the fall. Of course, the loss of wealth will have some adverse impact upon consumer and investor spending and upon government initiatives. (South Carolina probably will have few new government initiatives in the new year). However, the substantial transfer of income to the impacted areas through insurance (about half the reinsurance is from foreign sources) and federal government programs will more than offset these negative impacts. In fact, I am assuming that public construction will be $4 billion higher at annual rates in the fall and through the first half of 1990 to replace damaged infrastructure. The utilities alone will be spending nearly $600 million to replace damaged facilities, which will add to investment expenditures. Housing will soar as destroyed property will be replaced. Indeed, the natural disasters probably will add nearly $4 billion annualized to fourth quarter activity and an additional $6 billion early in 1990.

What is not yet fully appreciated is the fact that the natural disasters have restricted supply and increased aggregate demand through insurance and government transfers. Although the magnitudes are not great, some increasing inflationary pressures should be expected. Certainly, building materials should rise in price. A price decline in aluminum was arrested by the incapacitation of a South Carolina smelter. Wages of construction workers probably will increase in the impacted areas. If reinsurance capacity has been impaired by the size of these insurance claims, as some people claim, insurance rates also will rise. Thus, inflation could be a few tenths of a percent higher because of the natural calamities. Of course, this also means that interest rates would be higher than they otherwise would have been. Thus, a slight spurt in rates during the next few months should not be a total surprise.

However, the macroeconomic implications of these disasters can be overstated. Except for some of our monthly patterns during the fall and winter months, Hugo and the San Francisco earthquake have not be significant contributors to our estimates of economic activity for next year.

Quarterly Profile of GNP

	1989-2	1989-3	1989-4	1990-1	1990-2	1990-3	1989 Annual	1990 Annual
Real:	2.7	2.8	1.9	1.7	1.0	3.1	2.9	1.7
Price:	4.6	2.9	4.2	4.5	4.7	4.4	3.9	4.3
Nominal:	7.3	5.8	6.3	6.3	5.9	7.7	7.0	6.1

Monthly Statistical Highlights

	Sept 1989	Oct 1989	Nov. 1989
Payroll Employment		+143,000	+171,000
Index of Hours Worked		+0.1%	+0.1%
Household Employment		+194,000	+149,000
Civilian Unemployment Rate		5.3%	5.3%
Personal Income	+0.0%	+0.3%	+1.0%
Savings Rate	5.1%	5.1%	5.6%
Personal Consumption	+0.3%	+0.3%	+0.6%
Retail Sales		-0.6%	+0.7%
Auto Sales		9.6*	9.7*
Housing Starts		+6.2%	+0.4%
Housing Permits		-1.8%	-2.0%
Construction Expenditures	-1.8%	+0.9%	+1.4%
Business Inventories	+0.5%	+0.4%	+0.5%
Orders for Durable Goods		-1.9%	+0.3%
Orders - Nondefense Capital Goods		+2.1%	+1.3%
Industrial Production		-0.1%	+0.3%
CPI		+0.5%	+0.3%
PPI		+0.2%	+0.3%
Consumption Deflator	+0.3%	+0.4%	+0.3%
Leading Indicators	-0.1%	-0.3%	-0.1%
Currency Index		-2.2%	-0.8%
Equity Index		-0.8%	-2.1%
Real GNP (annual rate)	+1.5%	+0.6%	+2.3%
M1 (annual rate)		+12.5%	+5.6%
M2 (annual rate)		+7.4%	+5.6%

* auto sales in millions

FINANCIAL MARKETS

Another sharp decline in equity values on October 13 caused the Federal Reserve to provide liquidity. As a result, short-term interest rates fell while investors sought quality, causing long-term government bond yields also to fall. Although the stock market decline appears to have been caused by a flaw in the trading mechanism whenever a stock has trading halted because of order imbalances with a significant price implication, some economists have begun to seek signs that the market tumble is indicating economic weakness. A surge in initial unemployment claims, although related to production disruptions from Hugo, and weakness in durable goods orders provided more than sufficient ammunition to argue that a recession may be approaching. As a result, bond prices have remained firm.

However, a significant supply of long-term bonds by the government for treasury and for thrift bail-out purposes should slow the rally. Also, as mentioned above, the natural disasters will add to inflationary pressures, if only by a small amount. Thus, inflation surprises probably will arise during the next two months. This should lead to some rise in interest rates in the fall. By the winter, however, some slowing in economic activity could lead to a decline in interest rates as corporate and household credit market pressures ease. Assuming no substantial adverse impact from foreign investors, interest rates should reach their lowest levels early in the year. Then, gradual strengthening in the economy along with gradual increases in inflationary pressures should lead to Federal Reserve restraint late next year. The result will be a return to rising long-term interest rates before year-end.

It should be noted that the yield curve will steepen significantly during the year. Early in the year, short-term rates should fall faster than long-term rates. Late in the year, inflationary fears should cause long-term rates to drift upward even as short-term rates remain low.

EQUITY MARKETS -Apparently, a failure to maintain trading in UAL following a disappointing takeover announcement led to price instability in the stock market on October 13. Although trading was halted in UAL, the index futures which included UAL as one of its components continued to trade. As a result, traders quickly recognized that the current prices for the index would fall sharply when UAL again resumed trading. Therefore, these traders sold futures contracts, causing those contracts to fall to a deficit relative to the quoted index. This gap caused program traders to buy the futures and sell the stocks. Of course, they could not sell UAL, but they sold a representative sample of the other stocks. As a result, the stock market fell sharply.

Normally, such program trading would increase the futures and eliminate the gap between prices in the two markets. However, with UAL halted, any attempt to raise future prices relative to spot prices for the indices brought more selling of futures. This pattern occurred a week later when another UAL announcement led to temporary suspension of trading in the stock. When trading resumed, the arbitrage opportunities disappeared and the market rallied strongly.

Obviously, the market overseers need to eliminate this discrepancy in future and spot prices for indices when trading is halted with significant price implications. Until adjustments are made, further price volatility can be expected.

Of course, the other side of this distortion is the fact that economic fundamentals were not causing a rapid deterioration in equity values. Unfortunately, as the economy slows, economic fundamentals will surface. Therefore, the stock market should lose value during the fall. As no full recession is anticipated, the correction should not be substantial.

Some consumer and building material stocks should buck the downward trend. By spring, a rebound in technology shipments should also be reflected in the prices of their equities. A stock market rebound than could be expected next summer.

EMPLOYMENT

	Payroll Employment		Index of Hours Worked		Household Civilian Employment		Civilian Unemployment Rate		Hourly Earnings	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	108101	108101	128.7	128.7	117113	117113	5.3	5.3	9.61	9.61
May	108310	108310	127.6	127.6	117215	117215	5.2	5.2	9.60	9.60
June	108560	108607	128.0	128.1	117541	117541	5.3	5.3	9.62	9.62
July	108793	108767	128.4	129.2	117743	117459	5.2	5.2	9.68	9.69
August	108884	108855	128.7	128.4	117929	117597	5.2	5.2	9.72	9.68
September	109125	109064	129.0	128.6	118115	117456	5.1	5.3	9.77	9.73
October	109316	109207*	129.1	128.7*	118328	117650*	5.1	5.3*	9.81	9.76*
November	109506	109378	129.3	128.8	118524	117799	5.1	5.3	9.85	9.81
December	109698	109555	129.5	129.0	118720	117975	5.1	5.4	9.88	9.85
January 1990	109843	109694	129.7	129.0	118896	118143	5.2	5.4	9.94	9.88
February	110015	109807	129.6	129.1	119046	118280	5.2	5.4	9.98	9.92
March	110187	109910	129.7	129.3	119195	118402	5.1	5.5	10.02	9.96
April	110326	110121	130.0	129.5	119353	118645	5.1	5.4	10.06	10.00
May	110469	110314	130.2	129.7	119517	118860	5.1	5.4	10.11	10.03
June	110615	110456	130.5	129.9	119668	119049	5.2	5.4	10.16	10.07
July	110736	110646	130.4	130.1	119814	119199	5.2	5.4	10.20	10.11
August	110881	110794	130.5	130.2	119966	119348	5.2	5.5	10.24	10.16
September	111026	110958	130.7	130.4	120118	119532	5.2	5.5	10.29	10.21

PERSONAL INCOME

	Personal Income		Wage & Salary		Personal Savings		Disposable Income		Personal Outlays	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	4.387	4.387	2.601	2.601	183.3	184.3	3.718	3.719	3.535	3.534
May	4.395	4.396	2.604	2.604	203.5	199.4	3.747	3.747	3.543	3.548
June	4.407	4.418	2.617	2.622	224.1	218.6	3.769	3.777	3.545	3.559
July	4.435	4.447	2.640	2.645	225.0	222.4	3.795	3.802	3.570	3.580
August	4.458	4.466	2.651	2.654	226.3	207.4	3.813	3.819	3.587	3.612
September	4.481	4.466*	2.662	2.672*	224.1	193.1*	3.831	3.815*	3.607	3.622*
October	4.503	4.483	2.680	2.683	234.6	195.5	3.850	3.828	3.615	3.633
November	4.527	4.529	2.698	2.700	232.7	216.6	3.871	3.870	3.638	3.653
December	4.551	4.554	2.716	2.716	230.8	218.2	3.892	3.890	3.661	3.672
January 1990	4.575	4.572	2.730	2.726	232.4	212.4	3.911	3.902	3.679	3.690
February	4.602	4.595	2.745	2.740	234.0	212.5	3.932	3.923	3.698	3.711
March	4.629	4.621	2.760	2.757	233.2	213.1	3.953	3.946	3.720	3.733
April	4.649	4.648	2.776	2.773	223.4	218.6	3.970	3.967	3.747	3.748
May	4.672	4.671	2.794	2.787	216.0	221.3	3.983	3.985	3.767	3.764
June	4.695	4.698	2.812	2.804	224.7	228.3	3.996	4.008	3.771	3.783
July	4.710	4.724	2.825	2.821	230.3	223.6	4.020	4.029	3.790	3.805
August	4.729	4.764	2.838	2.839	231.7	236.7	4.045	4.064	3.813	3.827
September	4.749	4.796	2.851	2.858	233.1	245.5	4.070	4.091	3.837	3.846

Fore. = August Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

CONSUMPTION

	Personal Consumption		Durables		Nondurables		Services		Consumption Real	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	3433.2	3432.1	477.3	477.4	1113.2	1112.9	1841.7	1841.8	2652.5	2652.4
May	3440.2	3445.0	467.7	466.5	1118.1	1126.7	1854.4	1851.9	2647.8	2651.5
June	3441.4	3455.4	466.0	469.1	1118.5	1125.0	1856.9	1861.3	2644.3	2657.1
July	3468.2	3476.5	468.5	472.5	1126.4	1129.8	1873.3	1874.3	2657.6	2668.1
August	3483.4	3508.3	470.1	495.4	1128.7	1126.1	1884.6	1886.8	2663.2	2694.5
September	3495.9	3518.3*	468.9	488.4*	1131.1	1132.0*	1895.9	1897.9*	2666.6	2694.3*
October	3509.8	3528.5	465.0	478.2	1136.5	1141.0	1908.3	1909.3	2667.0	2691.3
November	3531.3	3549.3	467.0	478.4	1142.3	1150.2	1922.0	1920.7	2671.2	2698.6
December	3552.8	3567.6	469.0	480.4	1148.1	1155.6	1935.7	1931.6	2675.3	2704.3
January 1990	3571.6	3585.1	469.7	481.6	1154.1	1160.2	1947.8	1943.3	2679.4	2708.2
February	3590.1	3605.6	471.2	484.6	1159.3	1165.9	1959.6	1955.1	2685.2	2713.5
March	3608.8	3627.6	472.9	489.4	1164.5	1170.9	1971.4	1967.3	2691.1	2720.1
April	3631.7	3642.8	477.2	487.1	1170.2	1176.3	1984.3	1979.4	2698.1	2720.1
May	3653.2	3657.5	478.6	488.5	1176.4	1177.7	1998.2	1991.3	2702.1	2720.8
June	3676.0	3676.8	481.3	488.2	1182.6	1185.2	2012.1	2003.4	2706.9	2724.7
July	3685.4	3698.2	473.9	492.2	1187.3	1190.4	2024.2	2015.6	2703.9	2731.4
August	3702.1	3719.8	473.7	497.6	1192.4	1195.0	2036.0	2027.2	2708.2	2737.2
September	3722.1	3737.5	477.0	498.7	1197.3	1199.4	2047.8	2039.4	2712.9	2738.8

RETAIL SALES

	Retail Sales		Non-Auto Durables		Auto (Million Units)		Nondurable Sales		Auto Sales	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	141.07	140.94	22.41	22.41	10.8	10.8	87.30	87.12	31.36	31.41
May	142.10	142.54	22.97	22.97	10.2	10.1	88.20	88.40	30.93	31.17
June	142.17	142.50	22.79	22.85	10.0	9.9	88.66	88.48	30.72	31.17
July	142.49	143.56	22.84	22.80	10.0	10.2	88.83	88.90	30.82	31.85
August	142.85	144.51	22.70	23.16	10.6	11.5	89.01	88.78	31.14	32.56
September	142.91	145.21	22.71	23.22	10.6	10.6	89.20	89.17	31.00	32.82
October	142.88	144.30*	22.80	23.33*	9.4	9.6*	89.62	89.88*	30.46	31.09*
November	143.57	145.27	22.88	23.44	9.7	9.7	90.08	90.60	30.61	31.23
December	144.26	145.93	22.96	23.45	9.8	9.8	90.54	91.03	30.76	31.45
January 1990	144.81	146.43	22.90	23.58	9.7	9.7	91.01	91.39	30.90	31.46
February	145.39	147.22	22.98	23.44	9.8	9.9	91.42	91.84	30.99	31.94
March	145.99	148.16	23.04	23.45	9.9	10.2	91.83	92.23	31.12	32.48
April	146.94	148.33	23.00	23.46	10.0	10.0	92.28	92.66	31.66	32.21
May	147.59	148.77	23.07	23.58	10.0	10.0	92.77	92.94	31.75	32.25
June	148.39	149.15	23.14	23.63	10.2	9.9	93.26	93.36	31.99	32.16
July	147.91	150.02	23.02	23.74	9.7	10.1	93.63	93.77	31.26	32.51
August	148.29	151.00	23.08	23.89	9.6	10.3	94.03	94.13	31.18	32.98
September	149.05	151.47	23.15	23.85	9.7	10.4	94.42	94.48	31.48	33.14

Fore. = August forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

CONSTRUCTION

	Housing Starts		Single Family Starts		Housing Permits		Construction Expenditures (Current)		Construction Expenditures (Real)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	1.343	1.343	1.029	1.029	1.334	1.334	415.8	414.8	345.0	346.5
May	1.309	1.308	0.977	0.977	1.347	1.347	418.2	420.4	346.2	351.8
June	1.400	1.406	0.975	0.972	1.300	1.308	414.7	416.9	342.7	349.0
July	1.404	1.420	0.989	1.026	1.305	1.281	419.5	414.5	345.0	346.0
August	1.422	1.332	1.005	0.992	1.315	1.328	421.4	421.8	344.8	348.3
September	1.439	1.263	1.021	0.971	1.332	1.296	423.8	414.4*	344.8	340.8*
October	1.445	1.341*	1.025	1.005*	1.329	1.273*	426.5	418.1	346.2	342.4
November	1.461	1.346	1.021	1.002	1.345	1.247	429.8	423.9	348.6	346.0
December	1.456	1.373	1.029	1.022	1.347	1.255	433.3	428.9	350.9	348.4
January 1990	1.443	1.351	1.025	1.003	1.328	1.244	434.5	428.8	350.4	346.9
February	1.461	1.374	1.028	1.016	1.343	1.283	436.2	428.9	349.8	345.9
March	1.478	1.380	1.031	1.022	1.351	1.277	438.1	428.1	349.6	344.1
April	1.485	1.380	1.033	1.013	1.366	1.293	440.1	430.3	350.1	344.5
May	1.481	1.407	1.038	1.033	1.374	1.302	442.4	432.1	350.6	344.8
June	1.477	1.422	1.036	1.048	1.365	1.317	445.3	430.4	351.7	342.4
July	1.466	1.427	1.031	1.046	1.355	1.313	448.0	436.9	352.5	346.2
August	1.474	1.438	1.025	1.050	1.366	1.331	449.3	439.6	352.1	347.0
September	1.482	1.456	1.020	1.062	1.378	1.357	451.4	442.3	352.4	347.4

	Non-Residential		Public Construction		Residential Construction	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	131.4	131.8	80.4	79.4	204.0	203.7
May	133.3	133.6	84.7	85.9	200.2	200.9
June	136.1	134.8	80.6	83.5	197.9	198.6
July	137.0	133.8	83.0	81.7	199.5	199.0
August	136.6	136.9	83.9	86.0	200.9	198.9
September	136.5	135.2*	84.8	83.7*	202.5	195.5*
October	137.1	137.3	83.8	83.8	205.6	197.0
November	137.7	139.5	83.3	86.5	208.8	197.9
December	138.4	138.2	82.9	88.3	212.0	202.4
January 1990	138.0	138.3	83.3	89.3	213.2	201.2
February	138.8	138.4	83.7	87.8	213.7	202.7
March	139.6	138.7	84.2	86.2	214.3	203.2
April	140.0	139.2	84.0	86.1	216.1	205.0
May	139.6	139.6	84.2	86.3	218.6	206.2
June	140.2	139.5	84.1	86.5	221.0	208.4
July	140.6	139.6	85.2	86.8	222.2	210.5
August	141.6	140.3	85.0	87.5	222.7	211.8
September	142.5	140.8	85.6	88.1	223.3	213.4

Fore. = August Forecast
C.E. = Current Expectations
* = This item and those beyond it are projections.

BUSINESS ACTIVITY

	Manufacturers' Inventories		Durable Goods Orders		Non-Defense Capital Goods Orders		Non-Defense Capital Shipments	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	363.5	363.5	129.37	129.37	40.39	40.39	34.60	34.60
May	365.1	365.1	123.68	123.52	37.29	37.29	34.53	34.53
June	366.2	366.5	124.19	125.14	37.39	39.15	34.59	34.76
July	369.3	370.8	125.43	122.03	36.69	41.45	34.82	34.26
August	371.3	371.8	126.17	126.83	36.73	37.16	35.03	36.16
September	373.2	373.6*	125.84	126.68	36.45	35.08	35.24	36.01
October	375.3	375.2	124.76	124.23*	35.64	35.82*	35.06	35.66*
November	377.4	377.0	124.43	124.65	35.24	36.27	34.93	35.78
December	379.5	378.7	125.89	124.74	35.82	36.62	35.12	35.93
January 1990	381.2	380.4	126.14	125.96	35.98	37.43	35.66	35.87
February	383.2	381.8	127.35	124.15	36.27	36.27	35.87	36.22
March	385.1	383.4	127.53	124.36	36.41	36.65	35.94	36.54
April	386.0	385.0	128.56	124.95	36.98	36.85	36.45	36.80
May	386.9	386.5	128.85	125.23	37.23	36.77	36.51	36.81
June	387.8	387.8	129.18	125.45	37.64	36.82	36.69	36.84
July	388.6	389.1	130.14	125.33	37.83	36.56	36.81	36.83
August	389.6	390.5	130.42	126.14	37.95	36.93	36.95	36.92
September	390.5	392.0	129.64	126.01	37.82	36.83	36.90	36.94

	Business Inventories		Defense Shipments		Industrial Production		Capacity Utilization	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	771.3	771.3	8.63	8.63	141.6	141.7	84.1	84.2
May	778.1	778.1	8.70	8.70	141.4	141.6	83.8	84.0
June	780.8	780.8	9.20	9.23	141.1	142.0	83.5	84.0
July	783.3	787.6	8.86	8.19	141.4	142.0	83.5	83.8
August	785.1	789.9	8.94	8.94	141.8	142.4	83.6	83.8
September	787.0	793.8*	9.02	9.32	142.2	142.3	83.7	83.6
October	792.6	797.2	9.06	8.95*	142.7	142.1*	83.8	83.3*
November	798.0	801.1	9.11	8.84	143.2	142.5	83.9	83.4
December	803.4	804.7	9.16	8.93	143.6	142.9	84.0	83.5
January 1990	806.5	809.3	9.12	9.00	143.1	143.3	83.3	83.6
February	809.5	811.2	9.15	9.06	142.5	143.4	82.7	83.5
March	813.6	814.8	9.19	9.09	142.5	143.1	82.4	83.1
April	817.9	818.2	9.12	9.05	143.0	143.3	82.5	83.1
May	822.2	821.6	9.07	9.10	143.6	143.7	82.6	83.2
June	825.4	824.4	9.08	9.11	144.1	144.0	82.6	83.2
July	825.8	827.2	9.16	8.84	143.3	144.3	82.2	83.2
August	826.1	830.0	9.30	9.11	142.8	144.4	82.2	83.0
September	826.5	833.3	9.45	9.22	142.9	144.6	82.1	83.0

Fore. = August Forecast
C.E. = Current Expectations
* = This item and those beyond it are expectations.

PRICES

	CPI-U (seasonally adjusted)		PPI Finished Goods (seasonally adjusted)		PPI-Industrial Commodities (unadjusted)		Estimated GNP Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	123.3	123.3	113.1	113.1	111.8	111.7	125.5	125.5
May	124.0	124.0	114.1	114.1	112.3	112.4	126.1	125.9
June	124.2	124.2	113.9	114.0	112.2	112.3	126.4	126.2
July	124.7	124.5	113.7	113.5	112.0	112.2	126.7	126.5
August	125.0	124.5	113.5	113.1	112.1	111.7	127.0	126.5
September	125.3	124.7	114.0	114.1	111.6	112.1	127.5	126.9
October	125.8	125.3*	114.3	114.3*	112.6	112.8*	128.0	127.5
November	126.2	125.7	114.6	114.6	112.9	113.0	128.5	127.9
December	126.6	126.1	114.9	114.9	113.3	113.4	129.0	128.3
January 1990	127.0	126.6	115.2	115.4	114.0	114.0	129.4	128.9
February	127.5	127.1	115.5	115.8	114.6	114.5	129.8	129.3
March	128.0	127.6	115.8	116.3	115.2	115.1	130.2	129.8
April	128.5	128.2	116.3	116.7	115.7	115.6	130.7	130.4
May	129.0	128.7	116.8	117.0	116.1	116.0	131.1	130.8
June	129.5	129.2	117.2	117.4	116.5	116.4	131.6	131.3
July	130.1	129.7	117.7	117.8	117.0	116.8	132.0	131.7
August	130.8	130.3	118.2	118.2	117.4	117.3	132.5	132.2
September	131.5	130.8	118.7	118.6	116.5	116.6	133.0	132.8

	Consumption Deflator		Consumer Durables		Consumer Nondurables		Consumer Services		Implicit Construction Deflator	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	129.4	129.4	111.0	110.9	122.8	122.8	140.0	140.0	120.5	119.7
May	129.9	129.9	110.9	110.7	123.6	123.6	140.4	140.5	120.8	119.5
June	130.1	130.0	111.1	110.9	123.4	123.5	140.8	140.7	121.0	119.5
July	130.5	130.3	111.3	111.2	123.5	123.2	141.3	141.3	121.6	119.8
August	130.8	130.2	111.5	111.5	123.6	122.6	141.8	141.7	122.2	121.1
September	131.1	130.6*	111.8	111.8*	123.8	122.8*	142.4	142.1*	122.9	121.6*
October	131.6	131.1	112.0	112.0	124.2	123.3	143.0	142.6	123.2	122.1
November	132.2	131.5	112.2	112.2	124.7	123.8	143.6	143.0	123.3	122.5
December	132.8	131.9	112.4	112.3	125.2	124.2	144.2	143.5	123.5	123.1
January 1990	133.3	132.4	112.4	112.4	125.6	124.6	144.8	144.1	124.0	123.6
February	133.7	132.9	112.6	112.6	126.0	125.1	145.4	144.7	124.7	124.0
March	134.1	133.4	112.7	112.8	126.5	125.6	146.0	145.3	125.3	124.4
April	134.6	133.9	113.0	113.1	127.1	126.0	146.6	146.0	125.7	124.9
May	135.2	134.4	113.3	113.4	127.6	126.4	147.2	146.6	126.2	125.3
June	135.8	134.9	113.5	113.6	128.0	126.9	147.8	147.2	126.6	125.7
July	136.3	135.4	113.7	113.8	128.4	127.3	148.4	147.8	127.1	126.2
August	136.7	135.9	114.0	114.1	128.7	127.8	149.0	148.4	127.6	126.7
September	137.2	136.5	114.3	114.4	129.1	128.4	149.6	149.0	128.1	127.3

Fore. = August Forecast
C.E. = Current Expectations
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MISCELLANEOUS

	Merchandise Trade Balance		Leading Indicators	Estimated GNP		Estimated GNP (1982 $)		IVA (annual rate)	
	Fore.	C.E.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	-8.29	-8 29	145.6	5175	5186	4124	4132	-35.3	-34.9
May	-8.83	-10.08	143.8	5197	5200	4121	4130	-18.4	-18.9
June	-8.71	-8.01	143.7	5211	5218	4123	4135	-15.3	-13.6
July	-8.73	-8.24	143.9	5246	5235	4140	4138	-19.9	-10.1
August	-8.45	-10.77	144.4	5273	5256	4152	4155	-20.1	- 3.7
September	-8.93	-9.00*	144.2*	5301	5279	4158	4160	-19.2	- 5.8
October	-8.66	-9.04	143.8	5334	5307	4167	4162	-20.6	-10.3
November	-8.73	-9.15	143.7	5367	5333	4177	4170	-21.4	-14.6
December	-8.81	-8.96	144.1	5399	5361	4185	4178	-23.3	-15.4
January 1990	-8.16	-8.52	144.3	5416	5395	4185	4185	-31.1	-19.1
February	-8.05	-8.43	144.2	5428	5419	4182	4191	-30.2	-20.6
March	-7.95	-8.46	144.1	5441	5441	4179	4192	-27.6	-22.5
April	-8.16	-8.47	144.6	5477	5474	4191	4198	-21.1	-22.2
May	-8.24	-9.65	144.8	5512	5501	4204	4206	-14.9	-23.8
June	-8.36	-8.06	145.0	5547	5529	4215	4211	-16.7	-26.6
July	-8.12	-8.21	145.3	5563	5558	4214	4220	-20.6	-25.3
August	-8.28	-9.23	145.6	5582	5592	4213	4230	-25.3	-24.7
September	-8.36	-8.43	145.4	5602	5623	4212	4234	-29.9	-24.5

	Currency Index		Adjusted Profits		30-Year Government Bonds		New York Composite	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	97.24	97.24	165.9	170.3	8.89	9.03	170.34	169.38
May	100.81	100.81	176.2	167.6	8.85	8.83	175.56	175.30
June	103.09	103.09	177.3	180.8	8.46	8.27	180.90	180.76
July	98.43	99.12	178.4	175.5	8.31	8.08	188.43	185.15
August	97.12	100.44	171.7	182.4	8.22	8.12	187.72	192.83
September	95.76	101.87	164.0	178.3	8.13	8.15	185.43	193.02
October	94.43	99.63*	168.5	170.5	8.18	7.96*	185.67	191.43*
November	94.82	98.84	170.4	173.6	8.12	8.12	183.19	187.43
December	95.36	97.63	172.1	177.4	8.15	8.01	180.74	187.08
January 1990	96.25	97.56	164.8	180.1	7.81	7.86	172.25	183.80
February	95.46	95.83	160.1	175.6	7.73	7.73	165.76	180.50
March	94.86	95.14	158.2	167.5	7.68	7.75	159.50	178.95
April	93.26	95.28	165.5	166.4	7.72	7.82	158.77	183.43
May	92.94	95.14	171.2	168.2	7.66	7.85	159.38	180.30
June	92.96	94.43	171.5	171.6	7.70	7.93	163.46	182.76
July	92.15	95.24	167.3	178.3	7.68	8.14	162.53	186.42
August	91.82	95.54	161.6	175.4	7.63	8.22	165.12	188.93
September	91.56	95.42	155.8	173.3	7.69	8.31	167.83	185.56

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FINANCIAL MARKETS

	Monetary Base		M1		M2		Federal Funds		T-Bills (6 Mos.)	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	289.1	289.0	783.1	783.1	3081.1	3080.8	9.84	9.84	8.65	8.65
May	289.0	289.0	773.3	773.3	3071.8	3072.2	9.81	9.81	8.39	8.39
June	289.6	289.7	770.5	770.3	3087.3	3088.0	9.47	9.53	8.04	7.93
July	290.9	290.4	777.2	777.3	3119.1	3117.6	9.23	9.24	7.89	7.61
August	293.8	290.9	783.2	777.7	3136.1	3136.5	9.11	8.99	7.63	7.74
September	296.7	291.7	787.4	781.8	3153.2	3156.4	8.99	9.02	7.70	7.74
October	298.0	292.4*	790.7	789.5*	3171.6	3175.3*	8.73	8.81*	7.75	7.63
November	299.2	294.0	794.4	793.1	3190.3	3189.8	8.77	8.75	7.79	7.56
December	299.9	295.3	797.8	796.9	3209.0	3205.2	8.70	8.76	7.80	7.59
January 1990	301.8	296.7	800.4	801.0	3223.6	3221.3	8.33	8.43	7.42	7.27
February	303.3	298.2	803.7	803.6	3237.2	3237.4	8.13	8.26	7.38	7.11
March	304.9	299.7	807.0	806.3	3250.9	3250.4	7.94	7.92	7.34	6.93
April	306.5	301.2	813.3	810.1	3272.1	3265.7	7.87	7.88	7.19	6.95
May	307.9	302.4	818.4	811.9	3294.0	3278.8	7.83	7.85	7.15	6.91
June	309.3	303.9	823.5	815.1	3315.8	3295.2	7.80	7.83	7.11	7.04
July	311.0	305.3	828.4	818.3	3331.6	3311.7	7.76	7.86	7.01	7.13
August	312.4	306.8	831.8	820.8	3352.5	3328.3	7.73	7.92	7.00	7.22
September	314.2	308.2	835.1	823.1	3373.3	3344.9	7.79	7.93	7.06	7.27

	Aaa (Seasoned)		Municipals (Bond Buyer)		(3 Month) Commercial Paper		90 Day CD's		Prime Rate	
	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.	Fore.	C.E.
April 1989	9.79	9.79	7.49	7.49	9.81	9.81	9.94	9.94	11.50	11.50
May	9.57	9.57	7.25	7.25	9.47	9.47	9.59	9.59	11.50	11.50
June	9.20	9.10	7.03	7.02	9.12	9.11	9.32	9.20	11.07	11.07
July	8.99	8.94	6.85	6.96	9.17	8.68	9.35	8.76	10.83	10.98
August	8.95	8.96	6.84	7.06	9.05	8.57	9.26	8.64	10.50	10.50
September	8.90	9.01	6.80	7.26	8.96	8.70	9.15	8.78	10.50	10.50
October	8.90	8.88*	6.81	7.17*	8.70	8.63*	8.91	8.74*	10.50	10.50*
November	8.83	8.95	6.73	7.25	8.76	8.71	8.97	8.76	10.50	10.50
December	8.76	8.93	6.67	7.23	8.68	8.68	8.92	8.74	10.50	10.50
January 1990	8.63	8.76	6.55	7.08	8.26	8.26	8.52	8.38	10.03	10.23
February	8.57	8.65	7.48	7.01	8.08	8.14	8.23	8.22	9.57	10.00
March	8.43	8.72	6.35	7.09	7.88	7.78	8.05	7.91	9.50	9.83
April	8.56	8.81	6.46	7.19	7.79	7.75	7.93	7.90	9.50	9.50
May	8.63	8.84	6.54	7.22	7.85	7.76	7.99	7.91	9.50	9.50
June	8.60	8.93	6.55	7.30	7.84	7.72	7.98	7.86	9.50	9.50
July	8.46	9.02	6.41	7.38	7.71	7.74	7.89	7.87	9.50	9.50
August	8.39	9.14	6.35	7.45	7.75	7.83	7.92	7.95	9.50	9.50
September	8.50	9.22	6.49	7.66	7.82	7.95	7.97	8.12	9.50	9.78

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